Supreme Court, U.S.
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No. 91-1973

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

MICHAEL K. TOPALIAN, WARREN B. FIENGA, ROY JACOBS, JR., RICHARD OROZCO, JUAN GARCIA-QUIROGA, JEAN STUEBING, CHARLES W. ANDERSON, FRANCIS D. COVERT, RICHARD H. MANUEL, JACK E. BURROUGHS, DON W. BOYETT, BOBBY W. McDONALD, CHARLES F. LACELLE, RICHARD D. MIKLES AND MJM VENTURES,

Petitioners,

v.

JOHN N. EHRMAN, EHRMAN INVESTMENT GROUP, INC., W. RODERICK JOHNSON, W. RODERICK JOHNSON, P.C., RICHARD O'DONNELL, HOUSTON PETROLEUM CO., INC., JOEL A. MIDDLEBROOK, JOEL A. MIDDLEBROOK, CPA, VICTOR B. RUSSEK, RUSSEK CO., BERT GAMBLE, RIO BRAVO OIL CO., INC., ROCKWOOD INSURANCE CO. AND ROBERT E. ECKIS, JR.

Respondents.

Petition For A Writ of Certiorari To The United States Court Of Appeals For The Fifth Circuit

HOUSTON PETROLEUM CO., INC. AND RICHARD O'DONNELL'S ("RESPONDENTS") BRIEF IN OPPOSITION

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QUESTION PRESENTED

1. Whether the District Court's granting of summary judgment in favor of Houston Petroleum Company and Richard O'Donnell, and the Fifth Circuit Court of Appeals' affirmation of that decision, was proper when Petitioners failed to present any competent evidence or specific facts tending to establish a genuine issue for trial.

INTERESTED PARTIES

PETITIONERS

MICHAEL K. TOPALIAN, WARREN B. FIENGA, ROY JACOBS, JR., JUAN GARCIA-QUIROGA, RICHARD OROZCO, JEAN STEUBING, CHARLES W. ANDERSON, FRANCIS COVERT, RICHARD H. MANUEL, BOBBY W. McDONALD, JACK E. BURROUGHS, DON W. BOYETT, CHARLES F. LaCELLE, RICHARD MIKLES, and MJM VENTURES

RESPONDENTS

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NO. 91-1973

IN THE

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Petitioners,

v.

JOHN N. EHRMAN, EHRMAN INVESTMENT GROUP, INC., W. RODERICK JOHNSON, W. RODERICK JOHNSON, P.C., RICHARD O'DONNELL, HOUSTON PETROLEUM CO., INC., JOEL A. MIDDLEBROOK, JOEL A. MIDDLEBROOK, CPA, VICTOR B. RUSSEK, RUSSEK CO., BERT GAMBLE, RIO BRAVO OIL CO., INC., ROCKWOOD INSURANCE CO. AND ROBERT E. ECKIS, JR.,

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Petition For A Writ Of Certiorari To The United States Court of Appeals For The Fifth Circuit

HOUSTON PETROLEUM CO., INC. AND RICHARD O'DONNELL'S ("RESPONDENTS") BRIEF IN OPPOSITION

STATEMENT OF THE CASE

Respondents Houston Petroleum Company ("HPC") and Richard O'Donnell ("O'Donnell") adopt and incorporate by reference for all purposes Rio Bravo Oil Company, Inc.'s ("Rio Bravo") and Bert Gamble's ("Gamble") Brief in Opposition to Petitioners' Petition for a Writ of Certiorari regarding the factual background, procedural background, and reasons the petition should be denied except as expressly stated otherwise herein. HPC stands in very similar shoes as Rio Bravo in that HPC is an oil and gas operator that entered into contractual agreements with Onshore permitting Onshore to invest in wells to be drilled by HPC. Likewise, O'Donnell is the president of HPC and stands in similar shoes as Gamble who is president of Rio Bravo. For these reasons, many of the facts and arguments set forth in Rio Bravo and Gamble's brief in opposition apply equally to HPC and O'Donnell. Petitioners have also failed to raise any special or significant reasons to warrant granting their petition for writ of certiorari with respect to HPC or O'Donnell.

A. Factual Background

Like Rio Bravo, HPC's only connection with Onshore is a contractual relationship whereby HPC and Onshore entered into agreements permitting Onshore to invest in wells to be drilled by HPC. Petitioners have not alleged that HPC and O'Donnell failed to actually drill on certain agreed upon sites. Unlike many of the oil and gas programs promoted during the early 1980's, Onshore is a program that actually drilled and recovered oil and gas and has made payments to the Petitioners. Petitioners are merely dissatisfied because their investment strategy to get rich from an investment that looked lucrative in 1984 did not turn out quite as planned.

Neither HPC nor O'Donnell were involved in the promotion, offering, or sale of any interests in Onshore nor were they investors, partners, or owners in any interests of Onshore. Petitioners, as plaintiffs below, brought suit against HPC and O'Donnell, among others, alleging violations of federal and state securities laws, the Racketeer Influenced & Corrupt Organizations Act ("RICO"), and common law fraud. The undisputed and uncontroverted evidence produced to the District Court established that HPC and O'Donnell were not involved in the selling of limited partnership interests in Onshore nor did they make any representations, misrepresentations, or omissions of fact to any potential investor in Onshore. This evidence further established that neither HPC nor O'Donnell were involved in any RICO activities. This uncontroverted evidence was gleaned from extensive discovery that took place for over eighteen months after suit was filed and included numerous depositions of Petitioners, Respondents, and other witnesses.[1] Petitioners failed to provide any deposition testimony, counter-affidavits, or other competent evidence in their Response to Houston Petroleum Co., Inc. and Richard O'Donnell's Motion for Summary Judgment ("Response") that controverted or refuted the evidence produced by HPC and O'Donnell in support of their Motion for Summary Judgment.[2]

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1. Sworn affidavits were also provided as evidence supporting HPC and O'Donnell's Motion for Summary Judgment.

2. A copy of HPC and O'Donnell's Motion for Summary Judgment (without deposition exhibits) is provided in the Appendix to Respondents' Brief as H.1-H.39 Petitioner's Response to HPC and O'Donnell's Motion for Summary Judgment (with one exhibit attached) is provided in the Appendix to Respondent's brief as H.40-H.56. A copy of the supporting affidavit of O'Donnell is attached as H.35-H.38. All references to the Appendix are designated by an "H." preceding the page number.

B. Procedural Background

Like Rio Bravo and Gamble's motion, HPC and O'Donnell's Motion was supported by competent evidence in the form of sworn affidavits and deposition excerpts. The affidavit of Richard O'Donnell contained testimony that neither HPC nor O'Donnell (1) participated in any way in the preparation of the offering materials or prospectus promoting Onshore; (2) had any involvement with the selling activities undertaken on behalf of Onshore nor were they aware of the sales efforts made; (3) played any role in the offering of securities to Petitioners or any other investors, made any representations to any Petitioner, had any contact with any investor prior to their investments, or even knew any Petitioner's identity prior to the filing of the lawsuit; (4) played any part in or have control over the operation or management of Onshore; (5) had any control of any Onshore officer or employee or had any control over any of the policies, management, decisions, or any aspects of the business of Onshore; (6) were aware of any fraud or alleged fraud of any party perpetrated or sought to be perpetrated against any investor nor intended to render any assistance in any alleged fraud; (7) involved in or participated in any RICO activities or enterprise; (8) attempted to control any RICO enterprise or acquire an interest in or maintain an interest in a RICO enterprise; (9) participated in any racketeering activity; (10) obtained a financial interest in Onshore; (11) had any control over the affairs of Onshore; (12) had any position with Onshore that facilitated the perpetration of any alleged predicate acts; or (13) knowingly or wilfully become part of any alleged conspiracy. (H.35-H.38). Deposition testimony was also produced in support of the facts set forth in O'Donnell's affidavit and referenced in Respondents' Motion. (H.11, H.13, H.16-H-17, H-23, H.29). In addition, uncontroverted deposition testimony of the Petitioners established that neither HPC nor O'Donnell

made any statements to Petitioners in the offering or selling of interests in Onshore. *See* H.11, H.16-H.17, H.23. Therefore, the evidence produced by HPC and O'Donnell in support of their Motion was not only competent but also specific and substantial.

On July 26, 1989, Petitioners filed an untimely response to HPC and O'Donnell's Motion which the District Court graciously considered. (H.40-H.52). Petitioners' Response was filled with statements that the evidence produced at trial "will establish" Respondents' "culpability" and "will establish" that Respondents were participants in a scheme to defraud Petitioners. (H.43, H.46-H.47, H.49-H.51). Petitioners also asserted that they "must be given the opportunity to prove" Respondents participated in the alleged scheme and that they "will show at trial" or "will be able to show" at trial how Respondents engaged in this alleged scheme. (H.46-H.47, H.49-H.51). No evidence, competent or otherwise, was produced to the District Court to refute or controvert the specific, competent, and sworn testimony produced by HPC and O'Donnell in support of their Motion. The only "evidence" produced at all that refers to HPC is an unsworn and unsigned "stream of consciousness" letter that makes a single reference to HPC as "crooks."[3] (H.53-H.56). This, as the District Court stated, proves nothing. Petitioners failed to produce *any* sworn evidence through affidavits or deposition testimony to controvert the evidence produced by HPC and O'Donnell. As a result, the District Court granted HPC and O'Donnell's Motion and the Fifth Circuit panel affirmed that decision. Any additional "evidence" Petitioners seek to have this Court review is equally without competence and is not properly before this Court.

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3. Nowhere in the letter is Richard O'Donnell mentioned or even referenced.

REASONS THE PETITION SHOULD BE DENIED

Without burdening this Court with cumulative arguments and authorities, HPC and O'Donnell adopt and incorporate by reference for all purposes the arguments and authorities set forth in Rio Bravo's and Gamble's Brief in Opposition to Petitioners' Petition for a Writ of Certiorari. The exact same allegations made against Rio Bravo and Gamble are made against HPC and O'Donnell. Similar evidence and proof that was produced by Rio Bravo and Gamble in support of their motion was produced by HPC and O'Donnell in support of their Motion. Petitioners similarly failed to produce any evidence or proof in their Response to refute or contradict the evidence produced by HPC and O'Donnell.

Petitioners have also alleged violations of the RICO statute against HPC and O'Donnell. These points are more thoroughly addressed in Respondents' Brief to the United States Court of Appeals for the Fifth Circuit and Respondents' Motion for Summary Judgment. Both are incorporated for all purposes and attached in the Appendix hereto. (H.1-H.39, H.57-H.121).

The only "evidence" presented to the District Court in Petitioners' Response was an unsigned and unsworn letter. (H.53-H.56). This letter is not only incompetent summary judgment evidence since it is unsworn, unverified, and unsigned, but the letter does not state any specific facts tending to show that there is a genuine issue for trial. Nowhere in the letter does it have any specific facts or statements implicating HPC or O'Donnell in any alleged RICO enterprise, violation of securities law, or scheme to defraud investors in Onshore. As the District Court held, this proves nothing. Even assuming this letter is competent evidence, it is not specific nor sufficient to raise a genuine

issue for trial. For these reasons, and in accordance with this Court's decision in ***Celotex Corp. v. Catrett***, 477 U.S. 317 (1986), Petitioners petition should be denied.

CONCLUSION

The judgment of the District Court and subsequent affirmation by the Fifth Circuit Court of Appeals involves no unsettled questions of law and is entirely consistent with the prior rulings of the Court and other federal circuit courts. The questions that Petitioners raise are neither special nor significant. Therefore, the petition should be denied.

Respectfully submitted,

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APPENDIX

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MICHAEL K. TOPALIAN, et al.,	§	
Plaintiffs,	§	
	§	Civil Action
vs.	§	No. 87-3826
	§	
JOHN N. EHRMAN, et al.,	§	
Defendants.	§	

MOTION OF DEFENDANTS HOUSTON PETROLEUM CO., INC. AND RICHARD O'DONNELL FOR SUMMARY JUDGMENT

Defendants Houston Petroleum Co., Inc. ("HPC") and Richard O'Donnell ("O'Donnell"), pursuant to Rule 56 of the Federal Rules of Civil Procedure, file this motion for summary judgment. In support thereof, HPC and O'Donnell would show as follows:

1. As more fully discussed in the accompanying Memorandum, HPC and O'Donnell are entitled to summary judgment on all claims because there are no genuine issues as to any material fact and there is an absence of any evidence to support plaintiffs claims.

2. As more fully discussed in the accompanying Memorandum, HPC and O'Donnell are entitled to summary judgment on plaintiffs' claims under the Securities Act of 1933 on the ground that they are not sellers within the meaning of the Act.

3. As more fully discussed in the accompanying Memorandum, HPC and O'Donnell are entitled to summary judgment on plaintiffs' claims under the Securities Exchange Act of 1934 on the ground that they made no representations or omissions of fact to plaintiffs.

4. As more fully discussed in the accompanying Memorandum, HPC and O'Donnell are entitled to summary judgment on plaintiffs' RICO claims on the ground that they did not engage in a pattern of racketeering activities by acquiring, investing or controlling a RICO enterprise. Moreover, plaintiffs have no standing to assert a RICO claim against HPC and O'Donnell because their damages do not arise by reason of such violation.

5. In further support of this motion, HPC and O'Donnell incorporate the Memorandum In Support of Defendants Houston Petroleum Co., Inc. and Richard O'Donnell's Motion for Summary Judgment.

WHEREFORE, HPC and O'Donnell respectfully request that the Court grant its motion for summary judgment, and enter an order that plaintiffs take nothing, and grant HPC and O'Donnell such other and further relief to which this Court may deem them justly entitled.

Respectfully submitted,

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This is to certify that a true and correct copy of the foregoing was mailed this 15 day of June, 1989, to:

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By_____
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IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MICHAEL K. TOPALIAN, et al., Plaintiffs,	§	
	§	Civil Action
vs.	§	No. 87-3826
JOHN N. EHRMAN, et al., Defendants.	§	

MEMORANDUM IN SUPPORT OF DEFENDANTS HOUSTON PETROLEUM CO., INC. AND RICHARD O'DONNELL'S MOTION FOR SUMMARY JUDGMENT

Houston Petroleum Co., Inc. ("HPC") and Richard O'Donnell ("O'Donnell"), two of the defendants in the above action, file this Memorandum in support of their motion for summary judgment and would show the following:

I.
BACKGROUND

Plaintiffs are dissatisfied investors in Onshore Exploration, Ltd., 1984 Mid-Year Drilling Program ("Onshore"), an oil and gas drilling limited partnership program. First Amended Complaint at 2-4 ¶ 1-5 ("Complaint"). These investments were highly leveraged tax shelters promoted by John Ehrman and Ehrman Investment Group. Wayne Byles was the original general partner in Onshore. In December 1984 he was succeeded by Rod Johnson and Ehrman Investment Group as co-general partners. Complaint at 8 ¶ 46; 9 ¶ 49. HPC is an oil and

gas operator that entered an agreement with Onshore to drill wells on certain sites. Complaint at 9 ¶ 49. O'Donnell is the President of HPC and has been sued individually and as President. Complaint at 1.

Unlike many of the oil and gas programs promoted during the early 1980s, Onshore is a program that actually drilled and recovered oil and gas and has made payments to the plaintiffs. *See* Complaint at 25 ¶ 110. In fact, Onshore continues in operation today. Plaintiffs are not dissatisfied because their promoter stole their money, the general partner is in bankruptcy, or no drilling was ever completed. Instead, plaintiffs are dissatisfied because their investment strategy to get rich from an investment that looked lucrative in 1984 did not turn out quite as planned. *E.g.*, Binder dep. at 45-46. Unfortunately, because of the inherent risk associated with oil and gas drilling, one of which is the price of oil and gas and the fact that such prices have plummeted since 1984, these programs did not turn out to be as immediately profitable as the plaintiff investors anticipated. Binder dep. at 45-46; Garcia-Quiroga dep. at 98, 101; Steubing dep. at 69-70, 107-08. Therefore, plaintiffs have brought this action claiming a laundry list of fraud and deception to get out of their investments. Complaint at 3-4.

Included among their claims are claims against HPC and O'Donnell for alleged violations of the federal and state securities laws, common law fraud and Racketeering Influenced & Corrupt Organization Act ("RICO"). The undisputed evidence establishes that HPC and O'Donnell were not involved in the selling of plaintiffs' limited partnership interests, made no misrepresentations or omissions of fact to the investors, and were not involved in any RICO activities. Thus, because there is a lack of evidence to support at least one essential element of each of the plain-

tiffs' claims, HPC and O'Donnell are entitled to summary judgment in their favor.

II.
STANDARD FOR SUMMARY JUDGMENT

Summary judgment is properly granted if the pleadings and evidence "show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). The Supreme Court recently clarified the burden of a party seeking summary judgment. In *Celotex Corp. v. Catrett*, 477 U.S. 317, 325 (1986), *cert. denied*, 108 S.Ct. 1028 (1988), the Supreme Court held that the moving party may discharge its burden by showing an absence of evidence to support the nonmovant's case. Thus, the Court stated, "Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Id.* at 322; *accord Fontenot v. Upjohn Co.*, 780 F.2d 1190, 1195 (5th Cir. 1986).

"Where the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, there is 'no genuine issue for trial.'" *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986). A mere scintilla of evidence in support of plaintiffs' position is not sufficient to survive summary judgment. Plaintiffs must point to particular evidence on which the jury could reasonably find in their favor. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 252 (1986). Furthermore, the nonmovant may not survive summary judgment by resting on mere allegations in their pleadings. *Isquith v. Middle S.*

Utils., Inc., 847 F.2d 186 (5th Cir.), *cert. denied*, 109 S.Ct. 310 (1988). The evidence in this case demonstrates that plaintiffs cannot establish each of the essential elements of the claims asserted against HPC and O'Donnell and therefore summary judgment in their favor is proper.

III.
HPC AND O'DONNELL DID NOT VIOLATE ANY PROVISION OF THE SECURITIES ACT OF 1933

Plaintiffs' allegations under sections 12 and 15 seek to impose liability on HPC and O'Donnell for alleged oral and written misrepresentations in connection with the sale of their partnership interests. Recent Supreme Court and Fifth Circuit precedents demonstrate conclusively that no liability for any violations of the Securities Act of 1933 can be leveled against HPC and O'Donnell because they do not meet the statutory definition of "seller" under the Act, and therefore they are entitled to summary judgment.

A. Elements of Section 12 and 15 Claims

Plaintiffs' Complaint contains vague, confusing and essentially meaningless cross-references that attempt to assert a cause of action under sections 12 and 15 of the Securities Act of 1933, 15 U.S.C. § 77(l), (o) (1982), against HPC and O'Donnell. Complaint at 29, 34 and 39. Section 12(1) provides a right of action against anyone who offers or sells a security in violation of § 77(e), which makes it unlawful to use interstate commerce as the means to sell a security unless a registration statement is in effect and the prospectus meets the requirement of the Act. 15 U.S.C. § 77(l)(1). Section 12(2) provides a private cause of action against any person who offers or sells a security through communications which include material misrepresentations or omissions of material facts. *Id.* § 77(l)(2). Section 15 provides a private right of

action against any person who controls any person liable under sections 12(1) or 12(2). *Id.* § 77(o). To come within the ambit of these statutory provisions, plaintiffs must establish that HPC and O'Donnell were "sellers" of their securities.[1]

B. HPC and O'Donnell are not "Sellers"

The Supreme Court redefined persons liable under section 12(1) of the Securities Exchange Act of 1934 in *Pinter v. Dahl*, 108 S.Ct. 2063 (1988), finding that the proper inquiry is into the relationship between the investor and the defendant; *not* the defendant and the transaction. *Id.* at 2080-81. In directing this inquiry, the Court specifically held that section 12(1) "imposes liability on the owner who passed title, or other interest in the security, to the buyer for value," as well as one who "engaged in solicitation." *Id.* at 2076. The Fifth Circuit, following *Pinter's* guidance, extended that definition of seller to cover claims asserted

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1 1.The statute of limitations applicable to actions under sections 12 and 15 is set forth in section 13, which provides that actions to enforce liabilities under sections 12 and 15 must be brought either within three years of the sale to plaintiffs, or within one year of the discovery of the fraud, whichever period is shorter. 15 U.S.C. § 77(m) (1982), *see Buder v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 486 F. Supp. 56 (E.D. Mo. 1980). In no circumstances may an action be brought more than three years after the security is purchased. Moreover, plaintiffs' sections 12 and 15 claims should be dismissed because section 13 provides that actions must be brought within one year of discovery or after "discovery should have been made by the exercise of reasonable diligence. ..." 15 U.S.C. § 77(m). Nowhere in the Complaint does any plaintiff allege when he discovered, or should have discovered the alleged fraud. A plaintiff must affirmatively allege compliance with section 13; failure to make such an allegation is grounds for dismissal. *See, e.g., Stewart Coach Indus., Inc. v. Moore*, 512 F. Supp. 879, 886 (S.D. Ohio 1981); *Kramer v. Scientific Control Corp.*, 352 F. Supp. 1175, 1176 (E.D. Pa. 1973).

under section 12(2) of the Act. *Abell v. Potomac Ins. Co.*, 858 F.2d 1104 (5th Cir. 1988). The Court of Appeals held that when a court examines any claim under section 12, two inquiries must be made: "(1) [w]ho passed title to the plaintiff or solicited the transaction in which title passed; and (2) from whom did the plaintiff buy the security?" *Id.* at 1114.

Every case citing to and following *Pinter* has expressly declared that a plaintiff must demonstrate that each defendant "actually solicited their investment" for section 12 liability to attach. *See, e.g., Capri v. Murphy*, 856 F.2d 473, 479 (2d Cir. 1988) (noting that Second Circuit precedent previously held that language of sections 12(1) and 12(2) is identical"); *accord Schlifke v. Seafirst Corp.*, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174 (7th Cir. Jan. 9, 1989) (holding that a bank that financed allegedly illegal oil and gas limited partnerships was not a "seller" since it did not actively participate in the solicitation of investors or engage in preparing the prospectus except for drafting the loan documents included therein); *Harelson v. Miller Fin. Corp.*, 854 F.2d 1141, 1142 (9th Cir.), *cert. denied*, 109 S. Ct. 274 (1988) (finding that salesman/agent of defendant corporation "solicited" sales of securities by presenting facts necessary to effectuate sale to purchaser and receiving compensation for bringing sale about); *In re Professional Fin. Management, Ltd.*, 692 F. Supp. 1057, 1064 (D. Minn. 1988) ("Under the *Pinter* standard, liability may be imposed against [defendants] if they were principals to the sale or otherwise assisted in the transfer of securities as brokers, and received financial benefit in return.").

Plaintiffs muster no support for a finding that either HPC or O'Donnell could be declared a seller under this standard. The record is clear that they in no way "passed title or other interest" to any plaintiff. Like the bank in

Seafirst, HPC or O'Donnell were not involved in the solicitation or sale of these interests. O'Donnell Affidavit, attached hereto as Exhibit A. In fact, the plaintiffs admitted during their depositions that HPC and O'Donnell had no part in the sale or their interest to them. Garcia-Quiroga dep. at 136; Boyett dep. at 86-87; Burroughs dep. at 22-23; McDonald dep. at 1066; Topalian dep. at 127; Steubing dep. at 151; LaCelle dep. at 144, 150, 156-57.

HPC was simply the drilling operator. The undisputed evidence establishes that HPC and O'Donnell were not involved in Onshore's selling efforts. HPC and O'Donnell had no contact with Onshore's sales personnel. O'Donnell's Affidavit. Likewise, there is no evidence to support the allegation that HPC and O'Donnell participated in the preparation of the prospectus or in any way promoted the program. Moreover, the record directly refutes the contention that anyone at HPC had any knowledge of Ehrman's sales tactics. O'Donnell Affidavit. The only evidence establishes the contrary: O'Donnell testified that no HPC personnel had any knowledge of or control over the means by which Ehrman or the Onshore salesmen marketed the limited partnership interests. Boyett dep. at 109; Garcia-Quiroga dep. at 159-60; Burroughs at 84-85; Steubing dep. at 166; Topalian dep. at 135-36; McDonald dep. at 1061; LaCelle dep. at 147-48.

Every passage of record testimony in this case refutes the assertion that HPC and O'Donnell engaged in the direction of or solicitation by Onshore's sales force. HPC and O'Donnell were not engaged in soliciting sales and therefore cannot be said to have been "sellers" of these interests for purposes of the 1933 Act. Plaintiffs' claims must be dismissed.

C. HPC and O'Donnell are not "Control" Persons Under the 1933 Act

HPC and O'Donnell's total lack of control removes from possibility any liability under either the primary, secondary, or "control person" provisions of the 1933 Act. Particularly instructive here is the new decision by the Seventh Circuit in *Schlifke v. Seafirst Corp.*, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174, at 91,592 (7th Cir. Jan. 9, 1989). In deciding that liability under the 1933 Act could not lie against defendant Seafirst, the court noted that:

> Although the Bank necessarily became involved in the transaction ... to the extent necessary to fully document and protect its loans and collateral, there is no evidence that [it] thereby intended to be making an investment or that it took any steps to induce any investment by [the borrower] with [the seller].
>
> Thus, we agree with the district court that the Bank was acting merely as a commercial lender when it extended a loan to ENI 1981-III at a fixed rate of interest.

Id. at 91,597 (citations omitted, ellipses in original).

The *Schlifke* court expressly refused to allow any cause of action based on "aiding and abetting" liability under section 12(2). *Id.* at 91,597-98. Likewise, in the recent decision of *Commins v. Johnson & Higgins, Inc.*, 1988 Fed. Sec. L. Rep. ¶ 94,092 (N.D. Cal. Sept. 28, 1988), the court explained that "control person" liability imposes liability "only a person who 'stands behind the scenes and controls the [securities violator] who is in a nominal position of

authority.'" *Id.* at 91,099 (quoting *Wool v. Tandem Computers, Inc.*, 818 F.2d 1433, 1441 (9th Cir. 1987)).

The record specifically negates any contention that HPC or O'Donnell played any part in the operation or management of Onshore. O'Donnell Affidavit; Boyett dep. at 109; Garcia-Quiroga dep. at 159-60; Burroughs dep. at 84-85; Steubing dep. at 166; Topalian dep. at 135-36; McDonald dep. at 1061; LaCelle dep. at 147-48. The evidence clearly shows that no HPC employee or officer directed or controlled any of the policies, management, decisions, people, or any other aspects of the business of Onshore, including any sales effort. O'Donnell Affidavit.

Thus, both the record testimony and the applicable legal principles make it clear that HPC and O'Donnell played no role in the operation of Onshore or in the sale or solicitation of plaintiffs' investment interests. HPC and O'Donnell did not direct or control any Onshore employee or operation. As such, HPC was merely the drilling operator for some of the wells, and cannot be found liable under the provisions of the 1933 Act.

IV.
HPC AND O'DONNELL DID NOT VIOLATE ANY PROVISIONS OF THE SECURITIES ACT OF 1934

Plaintiffs additionally assert that HPC and O'Donnell violated section 10(b) of the Securities and Exchange Act of 1934, and Rule 10b-5. Plaintiffs cannot recover under either theory because HPC and O'Donnell made no misrepresentation to plaintiffs, or any representation and owed no duty to disclose and therefore made no omission of fact.

A. Elements of Section 10(b) and 10b-5

Plaintiffs allege various violations of Section 10(b) of the Exchange Act of 1934 and Rule 10b-5. Section 10(b) provides an action by a purchaser or seller of "any security" against "any person" who used "any manipulative or deceptive device or contrivance" in connection with the purchase or sale of a security. 15 U.S.C. § 78(j)(b) (1982). Rule 10b-5 provides in material part:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.R.F. § 240.10b-5 (1983).

The purpose of a cause of action under § 10(b) and Rule 10b-5 is

> to protect persons who are deceived in securities transactions -- to make sure that buyers of securities get what they think they are getting and that sellers of securities are not tricked into parting with something for a price known to the buyer to be inadequate or for a consideration known to the buyer not to be what it purports to be.

Chemical Bank v. Arthur Andersen & Co., 726 F.2d 930, 943 (2d Cir.), *cert. denied*, 469 U.S. 884 (1984). The essential elements of a § 10(b) and Rule 10b-5 claim are (1) in connection with a securities transaction and (2) acting with scienter, the defendants made (3) a material misrepresentation or nondisclosure (4) upon which plaintiff relied and (5) thereby suffered injury. *Chemetron Corp. v. Business Funds, Inc.*, 718 F.2d 725, 728 (5th Cir.), *vacated on other grounds*, 460 U.S. 1007 (1983); *Pin v. Texaco, Inc.*, 1986 Fed. Sec. L. Rep. (CCH) ¶ 92,823, at 94,011 (5th Cir. July 14, 1986) (under § 10(b) essential element is misrepresentation or nondisclosure).

Most significantly, the plaintiffs must prove that "the defendant(s) acted with scienter, *i.e.*, with intent to deceive, manipulate, or defraud." *Hermann & MacLean v. Huddleston*, 459 U.S. 375, 382 (1983). The authorities are universal that this is a species of fraud. *See, e.g., id.* (§ 10(b) is a "catchall antifraud provision"); *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 472 (1977); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 203 (1976).[2] Moreover, as the

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2. In *Ernst & Ernst*, the Supreme Court refused to read a negligence or should have known standard in § 10(b) or Rule 10(b)-5 actions. The scienter requirement can be satisfied with a state of mind less than actual knowledge such as "sever recklessness." This standard requires a showing that the deception was "so obvious that the defendant must have been aware of it." *Warren v. Reserve Fund, Inc.*, 728 F.2d 741, 745 &

Supreme Court put it, "Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud." *Chiarella v. United States*, 445 U.S. 222, 234-35 (1980). No plaintiff can point to any fact in support of their allegation that the defendants were guilty of fraud. Burroughs dep. at 84-85; Garcia-Quiroga dep. at 159-60; Boyett dep. at 107-09, 111; LaCelle dep. at 161-62, 183; Steubing dep. at 165-67; Topalian dep. at 135-36; McDonald dep. at 1079. Accordingly, plaintiffs cannot establish an essential element of their 1934 Act claim.

B. HPC and O'Donnell Made No Representation to Plaintiffs

To recover under 10b-5, plaintiffs must establish that HPC and O'Donnell made a misrepresentation of material fact to them in connection with their purchase of these securities. *Abell v. Potomac Ins. Co.*, 858 F.2d 1104, 1115 (5th Cir. 1988). Plaintiffs cannot recover from HPC or O'Donnell for misrepresentation because the uncontroverted testimony of the plaintiffs establishes that neither HPC or O'Donnell made *any* statements, much less untrue statements, to them. McDonald dep., Vol. VI at 1062-66; Topalian dep. at 151; Garcia-Quiroga dep. at 159; Law dep. at 76; Burroughs dep. at 84-85; LaCelle dep. at 157-163, 168-69. The lack of statement is exemplified by plaintiff Mr. Bobby W. McDonald's testimony in deposition:

> Q. Do you have any information or evidence to indicate that Richard O'Donnell or HPC made any false representations to anybody to get them to buy Onshore units?
>
> A. No, sir.

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n.12 (5th Cir. 1984). In the present case, the plaintiffs are unable to meet even the lesser standard of "should have known."

McDonald dep. Vol. VI, at 1066. As a further example, plaintiff Charles F. LaCelle is unequivocal in his answers:

> Q. Do you have any facts that would show that HPC made any representations to you at all?
>
> A. Directly?
>
> Q. Directly or indirectly.
>
> A. No.
>
> Q. What about Mr. O'Donnell? Did he make any representations to you?
>
> A. No.
>
> Q. Would you have -- do you have any facts, or are you aware of any facts, that would show that HPC or Mr. O'Donnell assisted in any fraudulent misrepresentations that others may have made to you?
>
> A. No

LaCelle dep. at 161-62.

The failure of the plaintiffs to prove any untrue statement of material fact by HPC or O'Donnell requires that plaintiffs' 10b-5 claims be dismissed. *See Abell*, 858 F.2d at 1115-16.

C. HPC and O'Donnell Owed no Duty to Plaintiffs

The failure of a party to disclose facts constitutes actionable fraud only if the party had a duty to disclose the facts. *E.g., Chiarella v. United States*, 445 U.S. 222, 230 (1980); *Tempo Tamers, Inc. v. Crow-Houston Four, Ltd.*, 715 S.W.2d 658, 669 (Tex. App.--Dallas 1986, writ ref'd n.r.e.). Accordingly, the first step in analyzing plaintiffs' nondisclosure claims is to determine whether HPC and O'Donnell had a duty to disclose facts to plaintiffs.

First, as drilling operator, HPC and O'Donnell owed no fiduciary duty to the plaintiffs. A fiduciary relationship generally arises only from a relationship of trust and confidence. *Thigpen v. Locke*, 363 S.W.2d 247, 252-53 (Tex. 1962). A fiduciary relationship may be created from a variety of circumstances usually involving attorney-client, parent-child or some other special relationship; but generally it does not include relationships between businessmen dealing at arms length. *Consolidated Gas & Equip. Co. v. Thompson*, 405 S.W.2d 333, 336-37 (Tex. 1966). To allow the plaintiff investors to transform this arms length transaction between the drilling operator and the partnership to create a fiduciary duty from the operator to them would jeopardize the security of contracts in Texas. *See Thigpen*, 363 S.W.2d at 253. Thus, HPC and O'Donnell had no duty to disclose based upon a fiduciary duty.

Moreover, any action HPC undertook to assure itself of the viability of these programs for which it was about to act as drilling operator, lends no support to the conclusion plaintiffs wish to draw that HPC or O'Donnell owed plaintiffs any duty to disclose facts regarding their Onshore investments. *See Schlifke*, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174, at 91,599. As one court has noted, it is ludicrous

to contend that actions taken by a party in assessing its own risks in connection with a proposed transaction somehow translate into an affirmative duty to advise other participants in the transaction with regard to their decision whether or not to participate. *See National Union Fire Ins. Co. v. Eaton*, 701 F. Supp. 1031 (S.D.N.Y. 1988). In *Eaton*, the court found that the surety's review of the private placement memoranda for its own purposes did not require it to disclose any information to the investors. *Id.* The court noted that a surety has no duty to disclose adverse information it may have had. *See generally Delany v. Blunt, Ellis & Loewi*, 631 F. Supp. 175 (N.D. Ill. 1986) (citing *Woodward v. Metro Bank*, 522 F.2d 84 (5th Cir. 1975)); *Quintel Corp., N.V. v. Citibank, N.A.*, 589 F. Supp. 1235 (S.D.N.Y.) 1984); *Schlifke v. Seafirst Corp.*, 1987 Fed. Sec. L. Rep. (CCH) ¶ 93,107, at 95,443 (N.D. Ill. 1987), *aff'd* 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174 (7th Cir. Jan. 9, 1989); *In re Gap Stores Sec. Litig.*, 457 F. Supp. 1135 (N.D. Cal. 1978); *Ingenito v. Bermec Corp.*, 441 F. Supp. 525, 549 (S.D.N.Y. 1977).

Likewise, in *Schlifke*, the Court of Appeals refused to find any section 10(b) liability, stating that, "The bank had no communications with the investors and did not initiate the transaction or participate in it in any way that would induce the investors to rely on the bank to disclose information...." *Id.* at 91,600 (quoting *Jett v. Sunderman*, 840 F.2d 1487, 1493 (9th Cir. 1988)). Indeed, in discussing secondary 10(b) liability, the Seventh Circuit noted that routine extension of a loan does not satisfy the "substantial assistance" element. *Id.* at 91,601. The court concluded that "[e]ven affording the plaintiffs the benefit of all reasonable inferences, they had not sufficiently demonstrated that the [defendant] had 'thrown in his lot,' and ... 'joined common cause with other offenders or aided and abetted a scheme with the necessary

state of mind.'" *Id.* at 91,602 (quoting *Barker v. Henderson, Franklin, Starnes & Holt*, 797 F.2d 490, 497 (7th Cir. 1986)).

Plaintiffs also assert that even if HPC and O'Donnell were not engaging in primary fraud, they may have aided and abetted the primary fraud allegedly perpetrated by other defendants. Under the Fifth Circuit precedent, parties are subject to liability for aiding and abetting a securities violation only if the following elements are proved: (1) there must have been a security violation by the primary party; (2) the aider and the abetter must have had a "general awareness" of its role in a Rule 10b-5 violation; (3) the aider and abetter must have knowingly rendered "substantial assistance" in the Rule 10b-5 violation. *Abell*, 858 F.2d at 1126; *accord Bane v. Sigmundr Exploration Corp.*, 848 F.2d 579 (5th Cir. 1988); *Woodward v. Metro Bank*, 522 F.2d 84 (5th Cir. 1975).

To establish the "general awareness" element, plaintiffs must prove HPC and O'Donnell's knowledge of their role in a fraud, and their commitment (or intent) to aid in the fraud's success:

> Scienter, then would require first that the alleged abettor know of the fraud's existence and generally understand how its actions aid in promoting the success of the fraud. The second element of scienter-commitment would be met where evidence shows that the abettor acts from a desire to help the fraud succeed...
>
> If the evidence shows no more than a transaction constituting the daily grist of the mill, we would be loathe to find 10b-5 liabil

-ity *without clear proof of intent to violate the securities laws.*

Abell, 858 F.2d at 1127, (citing *Woodward*, 522 F.2d at 97) (emphasis added).

HPC and O'Donnell played no role in the offering of the securities. O'Donnell Affidavit. HPC nor O'Donnell knew of the existence of any alleged fraud. *See Bane*, 848 F.2d at 581. In *Bane*, the defendant was a lender who included loan documents in an investment package for an oil and gas limited partnership and made loans to some of the plaintiffs. *Id.* at 580. The court held that the inclusion of documents in investors packages and loaning money to the investors did not constitute substantial assistance for aiding and abetting liability under Rule 10b-5. *Id.* at 581.

In this case, HPC acted solely as the drilling operator. Thus, HPC was even more removed from the plaintiffs' investments than the surety, lender or escrow agent in *Eaton, Schlifke* and *Bane*. HPC did not review the investors' financial information and did not even know their identity until this lawsuit was filed. O'Donnell Affidavit. HPC had no contact or communication in even the most remote sense with any of the investors prior to their investment. O'Donnell Affidavit. HPC did not contribute to the prospectus. O'Donnell Affidavit. Although a copy of the agreement between Onshore and HPC was attached to the prospectus, as in *Bane*, this is not sufficient to reestablish substantial assistance. As plaintiffs admit in their Complaint, HPC's limited role was fully disclosed in the prospectus. Complaint at 12-14. Plaintiffs have no basis for asserting that HPC or O'Donnell had any duty to disclose, therefore, there is no basis for imposing liability on HPC or O'Donnell under section 10(b) and Rule 10b-5.

V.
HPC AND O'DONNELL DID NOT VIOLATE THE TEXAS SECURITIES LAW

Plaintiffs allege generally the HPC and O'Donnell's actions violated the Texas Blue Sky Securities Act, Tex. Rev. Civ. Stat. Ann. art. 581-33 (Vernon Supp. 1989). The elements necessary to establish a violation of the Texas Securities Act are substantially similar to those necessary to establish a violation of Rule 10b-5. Thus, a failure to prove a violation of Rule 10b-5 generally is considered a failure to prove a Texas Securities Act violation. *See Keasler v. Natural Gas Pipeline Co. of Am.*, 569 F. Supp. 1180 (E.D. Tex. 1983), *aff'd*, 741 F.2d 1380 (5th Cir. 1984); *Jeanes v. Henderson*, 688 S.W.2d 100 (Tex. 1985); *Sibley v. Horn Advertising Inc.*, 505 S.W.2d 417 (Tex. Civ. App.--Dallas 1974, writ ref'd n.r.e.), *cert denied*, 420 U.S. 929 (1975). Because plaintiffs cannot establish that HPC and O'Donnell violated Rule 10b-5, they likewise cannot establish a violation of the Blue Sky laws. Therefore, HPC and O'Donnell are entitled to summary judgment as a matter of law.

VI.
HPC AND O'DONNELL DID NOT COMMIT COMMON LAW FRAUD

Plaintiffs cannot recover against HPC or O'Donnell on a theory of common law fraud. The elements of actionable fraud in Texas are (1) that a material representation was made; (2) that it was false; (3) that, when the speaker made it, he knew it was false or made recklessly without any knowledge of its truth and as a positive assertion; (4) that they made it with the intention that it should be acted upon by the party; (5) that the party acted in reliance upon it; and (6) that he thereby suffered injury.

South Hampton Co. v. Stinnes Corp., 733 F.2d 1108 (5th Cir. 1984); *Trenholm v. Ratcliff*, 646 S.W.2d 927 (Tex. 1983). As discussed above, plaintiffs admitted in their depositions that neither HPC nor O'Donnell made any representations to them, or consequently any misrepresentations. McDonald dep. Vol VI at 1062-66; Topalian dep. at 151; Garcia-Quiroga dep. at 159; Law dep. at 76; Burroughs dep. at 84-85; LaCelle dep. at 157-63, 168-69. Because plaintiffs cannot establish the elements necessary to establish fraud, HPC and O'Donnell are entitled to summary judgment.

VII.
HPC AND O'DONNELL DID NOT VIOLATE THE RICO ACT

Plaintiffs assert RICO claims against HPC and O'Donnell based upon allegations of illegal kickbacks, and inflated contractual drilling prices. RICO prohibits four forms of activity: (1) investment in an enterprise engaged in or affecting interstate or foreign commerce of income obtained through a pattern of racketeering or through collection of an unlawful debt, (2) acquisition of an interest in such an enterprise through a pattern of racketeering or through collection of an unlawful debt, (3) conduct of the affairs of such an enterprise through a pattern of racketeering or through collection of an unlawful debt, and (4) conspiracy to violate any of these three provisions. Civil remedies are available for violations of section 1962 to persons injured "by reason of" such RICO activities. Plaintiffs' claims must fail because they cannot establish any of the essential elements of RICO and plaintiffs have no standing to assert RICO against HPC and O'Donnell.

A. Elements of a Civil RICO Case

The civil RICO statutes provide a private cause of action for any person injured in his business or property by reason of a violation of RICO. The injured person may seek redress for treble damages against the person or persons who caused his injury. 18 U.S.C. § 1964(c) (1982). To establish a RICO violation under any subsection of 1962, the essential elements are as follows: (1) a "person" (the defendant), (2) through the commission of two or more predicate acts, (3) constituting a "pattern" of "racketeering activity", directly or indirectly invests in (§ 1961(a)), or maintains an interest in (§ 1962(b)), or participates in (§ 1962(c)), an "enterprise", the activities of which affect interstate commerce, causing plaintiff injury in his business or property "by reason of" the defendants' activity. *Ocean Energy II, Inc. v. Alexander & Alexander, Inc.*, 868 F.2d 740, 742 (5th Cir. 1989); *Moss v. Morgan Stanley, Inc.* 719 F.2d 5, 17, 20-23 (2d Cir. 1983), *cert. denied*, 465 U.S. 1025 (1984). Plaintiffs' claims must fail because there is no evidence to support any allegation that HPC or O'Donnell engaged in a pattern of racketeering activities or that plaintiffs' injury was caused by such acts.

B. Plaintiffs Lack RICO Standing

Section 1964(c) authorizes a suit by any person injured in "his business or property *by reason* of a violation of § 1962." 18 U.S.C. § 1964(c) (1982). Thus, the Supreme Court has stated that anyone injured in his business or property as a result of a defendant engaging in a pattern of racketeering activity in a manner forbidden by § 1962 has a claim. *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 496-97 (1985). In a case presenting similar allegations as this one, the Fifth Circuit in construing RICO's standing requirement examined whether the plaintiffs were injured by

the conduct constituting the violation and whether the harm suffered was caused by the predicate acts. *See National Enters., Inc. v. Mellon Fin. Servs. Corp. No. 7*, 847 F.2d 251, 252-53 (5th Cir. 1988). In *Mellon*, the plaintiff creditor alleged it was injured by illegal kickbacks a company paid to its primary lender as a condition of financing, asserting that these kickbacks depleted the funds of the corporation which eventually declared bankruptcy. The Court found that the plaintiff's damages were too indirect, speculative and "beyond the pale of rational causation." *Id.* at 254. Thus, the court found the plaintiff lacked standing to assert a RICO claim.

In this instance, although plaintiffs' allegations are vague and somewhat unintelligible, they appear to claim that alleged kickbacks HPC made to Johnson, one of the general partners, and over charges it made to Onshore for drilling caused them injury. *See* Plaintiffs' Response to RICO Standing Order at 11, 31-33. Like in *Mellon*, plaintiffs who are investors in the limited partnership suffered no direct injury, if any, as a result of such alleged activity. Their injuries, if any, are too remote and speculative to have "flowed" from the commission of the predicate acts. *See Mellon*, 847 F.2d at 254, Therefore, they lack standing to assert RICO claims against HPC and O'Donnell.

C. Plaintiffs Cannot Establish the Existence of a Enterprise

Plaintiffs' claims must be dismissed because there is no proof to support their allegations that Onshore is the RICO enterprise. The existence of an "enterprise" is a crucial element of plaintiffs' RICO claim. *See Sedima*, 473 U.S. at 496-97; *United States v. Turkette*, 452 U.S. 576, 583 (1981). An "enterprise" includes any "individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact

although not a legal entity." 18 U.S.C. § 1961(4). The Supreme Court defined an "enterprise" in the context of § 1962:

> The enterprise is an entity, for present purposes a group of persons associated together for a common purpose of engaging in a course of conduct[,] ... proved by evidence of an ongoing organization, formal or informal, and by evidence that the various associated function as a continuing unit. ... The "enterprise" is not the "pattern of racketeering activity"; it is an entity separate and apart from the pattern of activity in which it engages.

452 U.S. at 583. The Fifth Circuit defined "enterprise" as requiring, in addition,

> the existence of a decision making structure, whether hierarchial or consensual. The RICO enterprise must have a common or shared purpose and continuity of structure and personnel.

Shaffer v. Williams, 794 F.2d 1030, 1032 (5th Cir. 1986) (citations omitted). To establish an "association in fact" enterprise, a plaintiff must show (1) an ongoing organization, formal or informal, (2) the association had a common purpose of engaging in a course of conduct, and (3) its various members functioned as a continuing unit. *Turkette*, 452 U.S. at 583; *Montesano v. Seafirst Commercial Corp.*, 818 F.2d 423,427 (5th Cir. 1987); *Shaffer*, 794 F.2d at 1032.

The Fifth Circuit recently elaborated on the distinction between the pattern and the enterprise:

> When the alleged section 1962(c) violator is a legal entity, such as a corporation, this required separation is not established merely by showing that the corporation, through its employees, officers, and/or directors, committed a pattern of predicate acts in the conduct of its own business. *Atkinson*. Nor does the fact that individual officers and employees of a corporation, in the course of their employment associate together and commit in the conduct of the corporation's business a pattern of predicate acts in its name and on its behalf, suffice to constitute such officers and employees (alone or together with the corporation itself) an association in fact enterprise distinct from the corporation. *Id*. And, in *Montesano* we also explained that a RICO plaintiff must plead specific facts that establish an association that exists other than merely to commit the predicate acts that show pattern. 818 F.2d at 427,

Old Time Enters., Inc. v. International Coffee Corp., 862 F.2d 1213, 1217-18 (5th Cir. 1989). The plaintiffs' allegations in their response to the Court's RICO Standing Order identifies the enterprise as Onshore. *See* Plaintiffs' Response to RICO Standing Order at 31 ¶ 6(a). There is no evidence to support the contention that Onshore functioned for the common purpose other than conduct of its own business. Neither is there any proof of any association-in-fact among the various defendants that includes HPC and

O'Donnell. O'Donnell Affidavit. Thus, plaintiffs cannot establish the existence of a RICO enterprise.

D. Plaintiffs Cannot Establish a Pattern of Racketeering Activity

Plaintiffs' RICO claims should be denied because they have not established that defendants committed a pattern of racketeering activity. A "pattern" or racketeering activity "requires at least two acts of racketeering activity." 18 U.S.C. § 1961(5) (1982). The Supreme Court in *Sedima* gave some insight to the "pattern" requirement:

> [A] pattern "*requires* at least two acts of racketeering activity, " § 1961(5) (emphasis added), not that it "means" two such acts. The implication is that while two acts are necessary, they may not be sufficient. Indeed, in common parlance two of anything do not generally form a "pattern," The legislative history supports the view that two isolated acts of racketeering activity do not constitute a pattern. As the Senate Report explained: "The target of [RICO] is thus not sporadic activity. The infiltration of legitimate business normally requires more than one 'racketeering activity' and the threat of continuing activity to be effective. It is this factor of *continuity plus relationship* which combines to produce a pattern." . . . of the same bill, Congress was more enlightening: "criminal conduct forms a pattern if it embraces criminal acts that have the same or similar purposes, results, participants, victims, or methods of commission, or otherwise are

> interrelated by distinguishing characteristics and are not isolated events."

473 U.S. at 496 n.14 (citations omitted)

Since *Sedima*, the great weight of authority has required a rigorous showing on this element. *See Smith v. Ayres*, 845 F.2d 1360, 1365-66 n. 18 (5th Cir. 1988); *Crocker v. FIDC* 826 F.2d 347, 348 n.2 (5th Cir. 1987), *cert. denied*, 108 S. Ct. 1075 (1988); *Montesano v. Seafirst Commercial Corp.*, 818 F.2d 423,426 (5th Cir. 1987); *Smoky Greenhaw Cotton Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 785 F.2d 1274, 1280-81 n. 7 (5th Cir. 1986), *cert denied*, 482 U.S. 928 (1987). Thus, plaintiffs must establish at least two predicate acts of racketeering activity, which are indictable as defined in the 18 U.S.C. § 1961(1)(A), that show "continuity plus relationship" with the legitimate business. *Old Time Enters., Inc.*, 862 F.2d at 1217. Plaintiffs' allegations fail to meet this "continuity plus relationship" test. Plaintiffs allege that HPC paid kickbacks to Johnson and over charged Onshore. There is no proof that these alleged acts were anything other than isolated instances.

Moreover, plaintiffs have no evidence that the alleged "predicate acts" constitute kickbacks or that HPC overcharged Onshore. RICO's definition of racketeering activity contains a laundry list of offenses which constitute the predicate acts necessary to establish a violation. 18 U.S.C. § 1961(1). Such acts must be acts "indictable" or "punishable" under one of several listed federal criminal laws or "chargeable" under a listed state law. *Id.* § 1961(1)(A). The alleged kickbacks were payments from HPC to Johnson arising from transactions wholly unrelated to Onshore. O'Donnell Affidavit. As Johnson testified the transactions transpired prior to his affiliation with Onshore. Johnson dep.

at 32, 35-36, 24. Johnson confirms that such payments were not kickbacks. Johnson dep. at 77. Likewise, the auditor hired to review HPC's books and records testified that he found no evidence that the payments were kickbacks. Leggio dep. at 242-44. Furthermore, the alleged overcharges are consistent with market prices and the contractual agreement in existence between Onshore and HPC. O'Donnell Affidavit. Thus, because plaintiffs cannot establish that HPC committed "predicate acts" that constitute a "pattern" or racketeering activity, HPC and O'Donnell are entitled to summary judgment.

E. Plaintiffs Cannot Establish the Activities Prohibited Under RICO

Plaintiffs cannot establish that HPC or O'Donnell derived income through a pattern or invested income, acquired or maintained an interest in, or controlled a RICO enterprise through a pattern of RICO activity. Therefore, their claims must fail.

To establish a violation of § 1962(a), the plaintiffs must establish that HPC and O'Donnell "derived income" from a "pattern" of "racketeering activity" in which they participated as principals; and that they used or invested that income to acquire an interest in, establish or operate the enterprise. *H.J., Inc.*, 648 F. Supp. at 428 n. 7. There is no evidence that either HPC or O'Donnell used or invested income derived from a pattern of racketeering activity in Onshore for any purpose. In fact, HPC and O'Donnell had no financial interest in Onshore. O'Donnell Affidavit.

Under 1962(b), the plaintiffs must establish that HPC and O'Donnell "acquired or maintained" an interest or "control" of the enterprise through a "pattern" of "racketeering activity." The object of the activity must be to

gain the interest or acquire control. Control is not limited by stock or capital ownership but may exist when the defendant has some meaningful ability to direct or influence the affairs or actions of the enterprise. *E.g., Sutliff, Inc. v. Donovan Cos.*, 727 F.2d 648, 653 (7th Cir. 1984). Again, there is no evidence that either HPC or O'Donnell gained an interest or controlled the affairs or actions of Onshore. The only evidence is to the contrary. O'Donnell Affidavit.

To establish a violation of § 1962(c), the plaintiffs must establish that HPC and O'Donnell were "employed by or associated with" the enterprise and "conducted" or "participated" in the conduct of the affairs of the enterprise through a pattern of racketeering activity. *Montesano*, 818 F.2d at 424. To satisfy the conduct element, the Fifth Circuit has held that the person must be able to commit the predicate offenses solely by virtue of his position in the enterprise, or the predicate offenses must be related to the activities of that enterprise. *United States v. Cauble*, 706 F.2d 1322, 1341 (5th Cir. 1983), *cert. denied*, 465 U.S. 1005 (1984). The *Cauble* court, adopted the following test:

> A defendant does not "conduct" or "participate in the conduct" of a lawful enterprise's affairs, unless (1) the defendant has in fact committed the racketeering acts as alleged; (2) the defendant's position in the enterprise facilitated his commission of the racketeering acts, and (3) the predicate acts had some effect on the lawful enterprise.

Id. at 1332-33. There is no evidence that HPC or O'Donnell had any position with Onshore that facilitated the commission of the alleged predicate acts. The only evidence is to the contrary. O'Donnell Affidavit. Thus, their claims must fail.

Section 1962(d) makes it unlawful to conspire to violate § 1962(a), (b), or (c). To establish a violation of § 1962(d), plaintiffs must establish that: (1) two or more persons entered into an unlawful agreement to violate § 1962(a), (b), or (c), as those offenses have previously been defined; (2) HPC and O'Donnell knowingly and willfully became members of the conspiracy; (3) HPC and O'Donnell agreed to commit at least two of the acts of racketeering activity alleged by plaintiffs to create a pattern; and (4) one of the members of the conspiracy knowingly committed at least one overt act in furtherance of the conspiracy alleged. *United States v. Cauble*, 706 F.2d at 1341; *United States v. Phillips*, 664 F.2d 971, 1012 (5th Cir. 1981), *cert. denied*, 459 U.S. 906 (1982); *United States v. Elliott*, 571 F.2d 880, 902-03 (5th Cir.), *cert. denied*, 439 U.S. 953 (1978). Plaintiffs must establish that HPC and O'Donnell objectively manifested intent to participate in the affairs of the enterprise. *Cauble*, 706 F.2d at 1341. There is no evidence that either HPC or O'Donnell knowingly and willfully became a member of any alleged conspiracy. The only evidence is to the contrary. *See* O'Donnell Affidavit.

VIII.
CONCLUSION

Wherefore, for the foregoing reasons, Houston Petroleum Co., Inc. and Richard O'Donnell urge this Court to grant their motion for Summary Judgment in its entirety.

Respectfully submitted,

OF COUNSEL: By: _____
Don Jackson

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ATTORNEY IN CHARGE FOR
DEFENDANTS HOUSTON
PETROLEUM CO., INC. and
RICHARD O'DONNELL

CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing was mailed this 15 day of June, 1989, to:

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By_____
Don Jackson

EXHIBIT A

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MICHAEL K. TOPALIAN, et al.	§	
	§	
V.	§	CIVIL ACTION NO.
	§	87-3826
JOHN N. EHRMAN, et al.,	§	

AFFIDAVIT OF RICHARD O'DONNELL IN SUPPORT OF HOUSTON PETROLEUM CO., INC. AND RICHARD O'DONNELL'S MOTION FOR SUMMARY JUDGMENT

THE STATE OF TEXAS	§	
	§	
COUNTY OF HARRIS	§	

Before me the undersigned authority on this day personally appeared RICHARD O'DONNELL, President of Houston Petroleum Co., Inc. ("HPC"), in the above-entitled and numbered cause and makes this affidavit in support of HPC and Richard O'Donnell's Motion for Summary Judgment, who, being duly sworn, deposes and says:

1. I am over 18 years old and am fully competent to make this affidavit. At all times relevant to this dispute, I have been the President of HPC, which is a Texas corporation doing business in the State of Texas with its principal place of business in Houston, Texas. In the transaction between Onshore Exploration, Ltd. 1984 Mid-Year Drilling Program and HPC, HPC acted as one of the oil and gas operators.

2. Neither HPC nor I participated in any way in the preparation of the offering materials or the prospectus that was put together to promote the program.

3. Neither HPC nor I had any involvement with the selling activities undertaken on behalf of the Onshore Exploration Program. We were unaware of the sales efforts that were made. We had no knowledge or control over the means by which the salesmen marketed the limited partnership interests.

4. Neither HPC nor I played any role in the offering of the securities to the plaintiffs or any other investors. As we were not involved in the offering of the securities, we made no representations, much less untrue statements, to any plaintiffs. Neither HPC nor I were involved in the soliciting of any investors to purchase an interest in the Onshore Exploration Program. Neither HPC nor I sold any investors their interests in this offering. We had no contact with the investors prior to their investments and did not advise them whether to purchase or whether this was a solid investment. We made no representations to the investors regarding the quality of this investment, about the program or otherwise. Neither HPC nor I reviewed the investors' financial information prior to their investment in the Onshore Exploration Program or at any time. We did not even know their identities until after the lawsuit was filed. Neither HPC nor I had any contact or communication in any sense with any of the investors prior to their investment.

5. Neither HPC nor I played any part in or had control over in the operation or management of Onshore. We did not control any Onshore Officer or employee, and we did not have any control over any of the policies,

management, decisions or any aspects of the business of Onshore, including but not limited to the sales efforts.

6. We were unaware and are still unaware of the existence of any fraud or alleged fraud by any party perpetrated or sought to be perpetrated against the investors and did not intent to render any assistance to any alleged fraud. We were and are unaware of how our actions would promote the success of any alleged fraud. We had no intent to violate any securities laws and did not violate any securities laws. We did not participate or intend to participate in any such fraud nor did we assist or intend to assist any such fraud succeed.

7. Neither HPC nor I were involved in any RICO activities. We did not participate in any RICO enterprise. We did not attempt to control any RICO enterprise, acquire an interest in, or maintain an interest in a RICO enterprise. To the best of my knowledge, Onshore is not a RICO enterprise nor is there any RICO enterprise associated with this drilling program.

8. Neither HPC nor I have participated in any pattern of racketeering activity. The payments HPC made to W. Roderick Johnson were not illegal kickbacks as plaintiffs alleged, but instead were commissions due to Mr. Johnson for transactions unrelated to the Onshore Exploration Program. HPC did not overcharge Onshore for exploration activities that it undertook. Instead, the prices charged are consistent with market prices and the contractual agreement in existence between Onshore and HPC. Neither HPC nor I had any financial interest in Onshore. Neither HPC nor I had any control over the affairs of Onshore. We did not have any position with Onshore that facilitated the perpetration of any alleged predicate acts.

9. Neither HPC nor I were knowingly or willfully a part of any alleged conspiracy.

/S/
RICHARD O'DONNELL

SWORN TO AND SUBSCRIBED BEFORE ME this 15 day of June 1989, by Richard O'Donnell.

/S/
Notary Public in and for the
State of Texas

(SEAL)

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MICHAEL K. TOPALIAN, et al., Plaintiffs,	§	
	§	Civil Action
vs.	§	No. 87-3826
	§	
JOHN N. EHRMAN, et al., Defendants.	§	

ORDER GRANTING HOUSTON PETROLEUM CO.,INC. AND O'DONNELL'S MOTION FOR SUMMARY JUDGMENT

This cause came before the Court on the Motion of Houston Petroleum Co., Inc. and Richard O'Donnell for Summary Judgment. The Court, having considered the motion and evidence on file, finds that there is no genuine issue as to any material fact and that defendants HPC and O'Donnell are entitled to judgment as a matter of law.

It is therefore, ORDERED, ADJUDGED AND DECREED that the motion of HPC and O'Donnell for Summary Judgment be and the same hereby is GRANTED. Plaintiffs shall take nothing by their action. This is a final judgment. All costs are assessed against the plaintiffs, jointly and severally.

Done this the _____ day of _____, 1989.

_____
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MICHAEL K. TOPALIAN, et al.,	§	
	§	
Plaintiffs,	§	
	§	Civil Action
VS.	§	No. 87-3826
	§	
JOHN N. EHRMAN, et al.,	§	
	§	
Defendants.	§	

PLAINTIFFS' RESPONSE TO THE HOUSTON PETROLEUM DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

To the Honorable Judge of said Court:

COME NOW **Michael K. Topalian, et al.,** Plaintiffs in the above styled and numbered cause, and file this their response in opposition to the Houston Petroleum Defendants' (**Houston Petroleum Company Inc.** and **Richard O'Donnell**) Motion for Summary Judgment.

The Houston Petroleum Defendants' Motion for Summary Judgment is friovolous. It represents a last-ditch effort by these Defendants to avoid a trial of this complex securities fraud and RICO case in which the evidence will clearly show that the Houston Petroleum Defendants and others engaged in acts and practices which operated as a fraud or deceit upon Plaintiffs in connection with the sale of securities.

Plaintiffs, in their First Amended Complaint (paragraphs 145 - 156), raise, in a clear and detailed manner, a number of serious allegations against the Houston Petroleum Defendants. The charges stem from the existence of a pre-Onshore attorney/client relationship between these Defendants and Onshore's second Managing general partner, Defendant W. Roderick Johnson and and his law firm, W. Roderick Johnson, P.C.

The nature of such a relationship is naturally suspect for allegations of conflict of interest and, in the instant case, as will be shown below, the relationship, in fact, led to self-dealings resulting in "kick-backs" (from the Houston Petroleum Defendants to the Johnson Defendants) in excess of ONE HUNDRED THOUSAND ($100,000.00) DOLLARS at the expense of Onshore and its investors, including Plaintiffs.

Plaintiffs' accusations are corroborated by the Johnson Defendants, themselves. In their February 11, 1988, Motion to Dismiss, the Johnson Defendants made the below quoted admissions relevant to Plaintiffs' allegations against the Houston Petroleum Defendants:

> "... As a result of an EIG-initiated audit,... EIG demanded and received an adjustment and a refund of moneys it had paid Houston Petroleum Company. In other words, **EIG WAS THE VICTIM OF SUCH ACTS AND EHRMAN AND EIG TOOK TIMELY ACTION... TO PROTECT THE INTERESTS OF THE HOLDERS OF THE LP UNITS."** (Emphasis added).

Defendant Joel A. Middlebrook, CPA and bookkeeper for the Partnership, also corroborates the Ehrman and

Johnson Defendants' position regarding the Houston Petroleum Defendants. In a January 22, 1986, letter to John N. Ehrman (Plaintiffs' Exhibit "A"), Ms. Middlebrook, in relevant part, states as follows with regard to the Houston Petroleum Defendants:

> "... I am surely disappointed that you did not use Bobby Steelhammer (a Houston attorney) to handle the settlement with Houston Petroleum as promised. Why not ???? He is a tiger, a good man to have in your corner when dealing with slick deal artists.
>
> I would like a copy of Rod's (Defendant Johnson) resignation as Managing General Partner of Onshore Exploration Ltd. 1984. You had told me that you had Bobby Steelhammer draw up his resignation papers, because you didn't want a thief in your midst.
>
> ... you have said that the cash investors are strictly for development deals. If that is true, **did you give the money to the crooks at Houston Petroleum????"** (Emphasis Added)

Deposition testimony, similarly corroborative, has been given by Onshore's geologist, Victor B. Russek, Jr., Onshore's original General Partner, Wayne M. Byles, Onshore's securities counsel, Frank Pinedo and Onshore's independent, certified internal auditor, Mr. Frank Leggio.

Moreover, Plaintiffs' extensive discovery in this case has revealed that the Houston Petroleum Defendants participated with Onshore's General Partners in a course of business which operated as a fraud on the Plaintiffs as investors.

Furthermore, Plaintiffs, at a minimum, can clearly establish that the Houston Petroleum Defendant aided and abetted the securities violations alleged in the Complaint. Plaintiffs again call the Court's attention to Defendant Joel Middlebrook who, on cross-examination by Houston Petroleum's attorney, testified in her deposition as follows at page 466 - 467:

Q. Do you recall a month or a year in your association with Onshore that you first became aware of Houston Petroleum Company?

A. It would have to be in the Fall of '84.

Q. How about Mr. O'Donnell? The same?

A. Same.

Q. And what was the occasion that brought about your learning of Houston Petroleum Company?

A. Well, one time I went to their office, before they started the program, and visited with them. **They had several people there that showed the office and what they were going to drill, and so on. It was a kind of dog-and-pony show for potential investors that John had set up and did.** (Emphasis Added)

Q. Okay. And were you by yourself?

A. Yes; I went by myself.

Q. You did? Was anyone else at the meeting besides...

A. Oh, yes; there were other people there.

Q. Okay. Who was there?

A. I don't know their names. They were just different prospective investors that showed up.

Q. Okay. Was Ehrman there?

A. Uh-huh.

Q. Okay. Anyone else associated with Onshore?

A. I don't remember. Rod may have been there; I'm not sure. He may or may not. I don't know; I doon't remember. **I know John was there; and a bunch of potential investors were there.** (Emphasis Added)

Q. **And who made the presentation for Houston Petroleum Company?** (Emphasis Added)

A. **One of their geologists**. I don't know his name. I have forgotten his name. (Emphasis Added)

Q. Was he the only individual who spoke?

A. No. I'm sure everybody had a little something to say.

Q. Do you recall the prospect that was presented at the time?

A. It was the one that was in the notebook, the Prospectus.

Q. You don't recall the name?

A. It was called the Thornton, No. 1 Thornton.

In this regard, Plaintiffs contend that the evidence shows that these Defendants had more than just a "general awareness" of their role in the Rule 10b-5 violations and that they knowingly rendered "substantial assistance" in the violations. *See Abell v. Potomac Insurance Co.*, 858 F.2d 1104, 1126 (5th Cir. 1988). Like Defendants Rio Bravo and Kelley Onshore, the Houston Petroleum Defendants disregarded the terms and conditions of the Memorandum and commenced drilling operations before Onshore funded.

Plaintiffs' claims under the RICO statute are equally strong in view of prevailing precedent. *See generally, H. J., Inc. v. Northwestern Bell Telephone Co.*, 57 U.S.L.W. 4951 (U.S. June 27, 1989), *reversing and remanding* 829 F.2d 648 (8th Cir. 1987); *Sedima, S.P.R.L. v. Imrex Company, Inc.*, 473 U.S. 479 (1985); *R.A.G.S. Couture, Inc. v. Hyatt*, 774 F.2d 1350 (5th Cir. 1985), *cited in H.J., Inc. v. Northwestern Bell Telephone Co., supra*, 57 U.S.L.W. at 4952 note 2.

Accordingly, the Houston Petroleum Defendants' contention that there is no genuine issue as to any material fact is on its face preposterous, especially given the complex facts of this case. If ever there was a case that was inappropriate for summary judgment, this is it. The Houston Petroleum Defendants' Motion for Summary Judgment is

clearly part of a large effort of certain Defendantsto avoid their day of reckoning by unnecessarily burdening Plaintiffs' counsel with paperwork. These Defendants' only hope at this point is that this Court will dismiss them from this lawsuit on any grounds possible so long as the ruling takes place prior to a trial on the merits. What Defendants want is a trial by deposition and affidavits; they fear the testimony that will be presented at trial which establishes their culpability. However, on this record, Plaintiffs are entitled to have this Court resolve the multitude of issues involving these Defendants in a trial on the merits.

1. **THE SECURITIES VIOLATIONS.** The Houston Petroleum Defendants assert that they had no duty to disclose anything to the investors because they lacked a fiduciary or other similar relationship of trust and confidence vis-a-vis the investors. They also deny liability for aiding and abetting securities laws violations, among other things.

The Houston Petroleum Defendants' contentions are without merit. Plaintiffs contend that the evidence will establish these Defendants' culpability in the scheme to defraud the Plaintiffs under Rule 10b-5. As the Fifth Circuit has noted, coverage under Rule 10b-5 is not a limited one. *Hilgeman v. National Ins. Co. of America*, 547 F.2d 298, 302 (5th Cir. 1977). The Rule, among other things, prohibits any person from engaging in "any act, practice or course of business which operates or would operate as a fraud or deceit upon any person." *Hilgeman, supra*, Section 240.10b-5.

Plaintiffs possess evidence which will establish that Defendants were participants in a scheme to enrich themselves and others at the expense of the Plaintiffs-investors. Plaintiffs will also be able to establish that the Houston Petroleum Defendants knowingly rendered

substantial assistance to others who violated Rule 10b-5.

Plaintiffs assert that the Houston Petroleum Defendants engaged in acts which operated as a fraud upon the Plaintiffs in connection with the selling of securities. At the trial on the merits, Plaintiffs will be able to clearly show that they suffered an injury as a result of deceptive practices "touching" the sale of securities to them within the meaning of Section 10b of the 1934 Securities Exchange Act. *Cf. Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 10-13 (1971).

Accordingly, Plaintiffs must be given the opportunity to prove that the Houston Petroleum Defendants not only aided and abetted violations of the securities laws but engaged in acts and business practices which operated as a fraud or deceit upon Plaintiffs in connection with their purchases of securities.

The Houston Petroleum Defendants' assertion that they had no duty to disclose anything to the investors is overbroad, inaccurate and without merit. As the Supreme Court stated in *Dirks v. SEC*, 463 U.S. 646, 655 n. 14 (1983), under certain circumstances even outsiders may become fiduciaries of investors where confidential information is legitimately revealed to an underwriter, accountant, lawyer, consultant or other persons solely for business purposes. That certainly, at a minimum, is the case here since Houston Petroleum Company was a joint-venturer in the project. Furthermore, it is also clear that one who misappropriates material information to his own advantage violates Section 10(b) and Rule 10b-5. *Cf. SEC v. Materia*, 745 F.2d 197, 203 (2d Cir. 1984); *Carpenter v. United States*, 791 F.2d 1024, 1027-1034 (2d Cir. 1986), *aff'd by an equally divided court on the 10(b) issue*, ___ U.S. ___ 108 S.Ct. 316, 320 (1987). Congress has now made clear

that liability is not dependent on a fiduciary relationship but applies to *any person* buying or selling while in possession of material undisclosed information and any persons communicating this information to others. *See "Insider Trading and Securities Fraud Enforcement Act of 1988"*, Sections 20A (a)(b)(c)(d) as amended, Pub. Law 100-704, 102 Stat. 4677 (November 11, 1988).

Accordingly, it is clear that there are many contested issues to be resolved with respect to the Houston Petroleum Defendants' liability under Rule 10b-5.

Similarly, there are numerous fact questions to be resolved concerning the Houston Petroleum Defendants liability under sections 12(1) and 12(2) of the 1933 Securities Act.

2. **RICO VIOLATIONS**. The Houston Petroleum Defendants' argument that Plaintiffs have failed to make out a RICO case against them is equally without merit. These arguments are particularly inappropriate here. Plaintiffs have gone to great lengths to plead this case with clarity and specificity. What Defendants are really requesting is that Plaintiffs prove their case in their Complaint.

Moreover, Defendants' memorandum conveniently omits any discussion of controlling cases that undermine their arguments. *See H. J., Inc. v. Northwestern Bell Telephone Co.*, 57 U.S.L.W. 4951 (U.S. June 27, 1989), *reversing and remanding* 829 F.2d 648 (8th Cir. 1987); *R.A.G.S. Couture, Inc. v. Hyatt*, 774 F.2d 1350 (5th Cir. 1985).

Throughout the text of their Complaint, Plaintiffs clearly detail that they were fraudulently induced to make sizeable investments of money in an "Enterprise" which was

conceived, developed and operated for the unjust enrichment of the Defendants. The "Enterprises" referred to are clearly the limited partnerships-Onshore Exploration Ltd., 1984 Mid-Year Drilling Program in one instance, and Texas Energy, Ltd., in the other. Thus, it is plain to see that Plaintiffs are not referring to Ehrman Investment Group, Inc., or any of the other Defendants as the "Enterprise."

Plaintiffs do contend, however, that Defendants Ehrman and Ehrman Investment Group, Inc. and the Houston Petroleum Defendants, inter alia, conducted or participated, directly or indirectly, in the limited partnership -- the Enterprise -- through a pattern of racketeering activity in violation of 18 U.S.C. 1962 (c). Plaintiffs will show at trial how the various Defendants constituted an association of organizations that regularly engaged in the practice of selling and financing investments in oil and gas limited partnerships through fraud, omissions of material facts and other unlawful acts.

To require Plaintiffs to conclusively prove these matters prior to trial is not required. However, Plaintiffs contend that they will be able to prove their case if given the opportunity.

Defendants' contention that Plaintiffs will not be able to show a pattern of racketeering activity is similarly without merit. In *R.A.G.S. Couture, Inc. v. Hyatt*, 774 F.2d 1350, 1354 (5th Cir. 1985), the Fifth Circuit read the "pattern and other requirements of the RICO Act broadly. The Court noted that the mailing of two (2) invoices alleged by plaintiff to be fraudulent was sufficient to constitude a pattern of racketeering activities". *R.A.G.S. Couture, Inc. v. Hyatt, supra*, 774 F.2d at 1354. The Supreme Court recently cited this case and holding in its most recent decision on RICO.

See H. J., Inc., v. Northwestern Bell Telephone Co., 57 U.S.L.W. 4951, 4952, n. 2 (1989).

In this case, Plaintiffs have alleged financial injuries as a result of various predicate acts, including violations of Section 10(b) and federal mail and wire fraud statutes. These allegations are sufficient to withstand a motion to dismiss. *Corwin v. Marney Orton Investments*, 788 F.2d 1063, 1069 (5th Cir. 1986). Moreover, Plaintiffs will be able to show "acts (on the part of Defendants) that have the same or similar purposes, results, participants, victims, or methods of commission," and that are otherwise "interrelated by distinguishing characteristics." *Sedima, S.P.R.L. v. Imrex Company, Inc.*, 473 U.S. 479, 496 at note 14 (1985). *Accord: H. J. Inc. v. Northwestern Bell Telephone Co.*, 57 U.S.L.W. 4951, 4953 (1989). Accordingly, Plaintiffs believe that they have a strong case against Defendants.

As the Fifth Circuit stated in *R.A.G.S. Couture, Inc. v. Hyatt, supra*, 774 F.2d at 1355:

> "The scope of the civil RICO statute is breathtaking. An allegation of fraud in a contract action can transform an ordinary state claim into a federal racketeering charge. It may be unfortunate for federal courts to be burdened by this kind of case, but it is not for this court to question policies decided by Congress and upheld by the Supreme Court." *Id.*

Plaintiffs contend that they will be able to prove their RICO allegations at the trial of this case under any of the standards referred to by Defendants in their memorandum. The acts of the Defendants in this case which were perpetrated against the Plaintiffs were the result of their

participation, directly or indirectly, in the affairs of the Parternship through a pattern of racketeering activity. Plaintiffs are entitled to their day in court in order to prove their case.

CONCLUSION

This difficult and complex case is clearly inappropriate for summary judgment. This is especially true for these Defendants since Plaintiffs are in the process of completing the deposition of Defendant Richard O'Donnell, president of Houston Petroleum Company. Due to conflicts in Mr. O'Donnell's attorney's trial schedule, Mr. O'Donnell's deposition has been re-scheduled on numerous occasions and was finally commenced on Friday, July 21,1989, and continued on Saturday, July 22, 1989. However, the deposition could not be concluded and Mr. O'Donnell's testimony will resume at a later date by agreement between counsel.

Factual issues abound with respect to every issue in this case. Congress has given this Court jurisdiction over defendants such as the Houston Petroleum Defendants and empowered this Court to award appropriate relief. Plaintiffs will be able to clearly establish at trial that the Houston Petroleum Defendants have played an important and substantial role in an intricate scheme to mislead and defraud investors for the personal gain of the Defendants. Plaintiffs are entitled to their day in court. Accordingly, Plaintiffs respectfully pray that the Houston Petroleum Defendants' Motion for Summary Judgment be denied.

Respectfully submitted,

/S/

Armando Lopez

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OF COUNSEL:

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(202) 686-6436

CERTIFICATE OF SERVICE

I, Armando Lopez, hereby certify that a true and correct copy of the foregoing instrument has been hand delivered to the Houston Petroleum Defendants, by and through their attorney of record, Mr. J. Don Jackson, VINSON & ELKINS, 3300 First City Tower, 1001 Fannin, Houston, Texas 77002, and by U.S. First Class Mail to all other counsel of record and pro-se parties on this the 7th day of July, 1989.

/S/
Armando Lopez

H53

January 22, 1986

Mr. John N. Ehrman
2 Northpoint Drive Suite 300
Houston, Texas 77060

Dear John:

I need a copy of the contract with Houston Petroleum which you told me about last week. I am surely disappointed you did not use Bobby Steelhammer to handle the settlement with Houston Petroleum as promised. Why not???? He is a tiger, a good man to have in your corner when dealing with slick deal artists.

I would like a copy of Rod's resignation as Managing General Partner of Onshore Exploration Ltd 1984. You have told me that you had Bobby Steelhammer draw up his resignation papers, because you didn't want a thief in your midst.

I would like to review the accounting records and bank records on Onshore for the year 1985. You have promised to give me the records since June 15, 1985. What is your problem in letting me look at them????

Please furnish a copy of run tickets and checks from HPC on the #1 through #4 Belt wells to date.

If you will provide me with a current partners list and the royalty bank account records. I will be able to prepare the 1099's for 1985. As you know, my royalty program is completed and we are able to print checks and maintain the necessary records.

Regarding Leggio, I called him to get a copy of the Houston Petroleum and Rio Bravo Audit reports. He said that he would see about getting a copy for me and that he incidentally, needed the Oil & Gas Reserves and Kelley Onshore contracts. You now have a copy of those contracts. I would, as a second request, like to have a copy of the audit reports.

The letter to Oil & Gas Reserves was asinine. Dick Manuel must be confused. I have not talked with Terry Richardson in a year and a half at least. The one person who called me was Hop Nolen. He is the primary person there. He is incidentally a client also. Your $350,000 hot check has been a problem to say the least.

Regarding reselling 15 Onshore units, where did you get your quantity?? Vic King is 3. Ernie is 1 or 2. You are telling me Barrow is the other 10. To date he has not received the $ from the sale of his units. And he has provided you with financing statements for his units.

This is my second request for the above information. If you don't have time to gather it, I will come out to help you get it together. You were supposed to leave a check for me yesterday. What happened????? I am seriously worried about what you have done. You are now telling me that you have only sold $1,500,000 in TEL. You are not supposed to break escrow until you have $2,400,000. Is this another occasion in which you do not exactly follow the prospectus guidelines, or are you trying to screw me out of the money per our letter agreement?????

You must not have the other $7,000,000 in cash investors or you would not have all those hot checks floating around. But, you have said that the cash investors are strictly for development deals. If that is true, did you give

the money to the crooks at Houston Petroleum???? Or does the money actually exist???? Where's the beef????

I have never known you to be niggardly about money. You must be in serious trouble on this deal, to get down to trying to short change me on this.

You have mentioned that you would like for me to cut you some slack on this deal. I will be happy to talk with you about it. Please tell me the truth about what you are doing. I have a hard time with a different story each week about what the deal is.

You are saying that you normally get 7 1/2% on the note finance deal. Your prospectus calls for a 3% general partner fee and a 4% sales commission. You pay out 3% to salesmen, retaining a total of 4%. If you sell the deal yourself, you keep a total of 7%. My 1/2% is equal to 12.5% of the 4% cash to the general partner. I will be happy to take 12.5% of the fee due you on the cash investors, since you receive 3% on those.

Thus, if you have $1,500,000 of note investors, you owe $7500 for those and for the cash investors of $7,000,000, you will owe $26,250, for a total of $33,750, rather than the full amount called for in our letter agreement, thus giving you a discount of $8750.

Per your letter of Monday, you say you aren't trying to short change me, that you haven't collected the funds due you. When you say you are going to leave a check for me

to collect when the funds are wired and you don't. I do feel you are trying to jack me around.

You have been rude, disloyal and untruthful in your dealings with me and others. I have never been involved in such a drill as this. As far as I am concerned, this will be the last deal we will ever be in together. I had looked forward to working with you in the oil programs. But, the way you run your business, I don't want to be involved.

Sincerely yours,

Joel A. Middlebrook

jne.186

EXH. "A"

H57

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NO. 90-2106

MICHAEL K. TOPALIAN, WARREN B. FIENGA, ROY JACOBS, JR., JUAN GARCIA-QUIROGA, RICHARD OROZCO, JEAN STEUBING, CHARLES W. ANDERSON, FRANCIS COVERT, RICHARD H. MANUEL, BOBBY W. McDONALD, JACK E. BURROUGHS, DON W. BOYETT, CHARLES F. LaCELLE, RICHARD MIKLES and MJM VENTURES

Plaintiffs-Appellants,

VERSUS

JOHN N. EHRMAN, Individually, Etc., et al.,

Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Texas

BRIEF OF HOUSTON PETROLEUM COMPANY and RICHARD O'DONNELL AS APPELLEES

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These Defendants-Appellees were served but never answered. Plaintiffs moved for a default judgment; however, the District Court denied Plaintiffs' motion and dismissed these Defendants from the litigation.

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Counter Plaintiff-Appellant ONSHORE EXPLORATION LTD. 1984 MID-YEAR DRILLING PROGRAM (ONSHORE)

ONSHORE (the Partnership) was not a party in the original suit now being appealed, but it was brought in as a Counter-Plaintiff by the EHRMAN Defendants. It is being represented by FRANK PINEDO, counsel for the EHRMAN Defendants.

STATEMENT REGARDING ORAL ARGUMENT

Appellees believe that although the issues presented by this appeal are clearly set forth and addressed in their brief, oral argument would be beneficial to this Court. Therefore, Appellees request oral argument.

EXPLANATION OF RECORD REFERENCES

A final record of this case has not been completed by the District Court. Attorneys for Houston Petroleum Company and Richard O'Donnell have contacted the clerk for the Fifth Circuit and were instructed to cite directly to the pleadings and documents referred to in their brief to this Court.

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IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NO. 90-2106

MICHAEL K. TOPALIAN, WARREN B. FIENGA, ROY JACOBS, JR., JUAN GARCIA-QUIROGA, RICHARD OROZCO, JEAN STEUBING, CHARLES W. ANDERSON, FRANCIS COVERT, RICHARD H. MANUEL, BOBBY W. McDONALD, JACK E. BURROUGHS, DON W. BOYETT, CHARLES F. LaCELLE, RICHARD MIKLES and MJM VENTURES

Plaintiffs-Appellants,

VERSUS

JOHN N. EHRMAN, Individually, Etc., et al.,

Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Texas

BRIEF OF HOUSTON PETROLEUM COMPANY and RICHARD O'DONNELL AS APPELLEES

TO THE HONORABLE JUDGES OF SAID COURT:

COME NOW, Houston Petroleum Company and Richard O'Donnell, as Appellees, and file this their response to the brief of the Appellants.

STATEMENT OF THE CASE

A. Proceedings and Disposition in the Court Below

This is an appeal from a final judgment entered against the Plaintiffs by the Honorable Judge Norman Black in the United States District Court for the Southern District of Texas, Houston Division. The Final Judgment provided that the Plaintiffs take nothing by way of their suit and was entered concurrently with an order granting summary judgment in favor of all Defendants. The Final Judgment and Order were signed by Judge Norman Black on October 4, 1989, and entered on the same date.

Plaintiffs are a group of investors in an oil and gas limited partnership known as Onshore Exploration Ltd. ("Onshore"), and have brought this action against numerous individuals and entities involved with or having some relationship with Onshore. Included among the Defendants is Houston Petroleum Company ("HPC") and Richard O'Donnell ("O'Donnell"). HPC is an oil and gas operator. HPC's only connection with Onshore is a contractual relationship whereby HPC and Onshore entered into agreements permitting Onshore to invest in wells to be drilled by HPC. O'Donnell's only connection is that he is the president of HPC.

Plaintiffs' Original Petition was filed in the United States District Court for the Southern District of Texas, Houston Division on December 3, 1987. On December 18,

1987, Plaintiffs filed their First Amended Complaint. The First Amended Complaint was Plaintiffs' operative pleading at the time summary judgment was granted. The Complaint alleged that Onshore's general partners and others defrauded Plaintiffs who purchased Onshore units. Specifically, Plaintiffs allege that Defendants violated various federal and state securities regulations, the Racketeering Influence and Corrupt Organization Act, and committed common law fraud.

On June 16, 1989, HPC and O'Donnell, along with other Defendants, filed a motion for summary judgment. Defendants HPC and O'Donnell filed their motion for summary judgment over eighteen months after the suit was filed and after numerous depositions and discovery had taken place. The depositions taken included many of the Plaintiffs, individual Defendants, Defendant entities, and other material witnesses. Based on this extensive discovery, Defendants HPC and O'Donnell's motion was filed asserting that there existed no genuine issue as to any material fact regarding any of the claims alleged against HPC or O'Donnell.

On July 26, 1989, Plaintiffs filed their response to this summary judgment motion. Although Plaintiffs' response to HPC and O'Donnell's motion was filed after the filing deadline, Judge Black graciously decided he would consider the Plaintiffs' response.

On October 4, 1989, HPC and O'Donnell's Motion for Summary Judgment was granted and a Final Judgment was entered providing that Plaintiffs take nothing. The District Court filed a supporting opinion within its order, including findings of fact and conclusions of law in connection with the Final Judgment. It is from this Final Judgment that Plaintiffs appeal.

B. Statement of the Facts

Plaintiffs are dissatisfied investors in Onshore Exploration, Ltd., 1984 Mid-Year Drilling Program ("Onshore"), an oil and gas drilling limited partnership program. First Amended Complaint at 2-4 ¶ 1-5 ("Complaint").[1] These investments were highly leveraged tax shelters promoted by John Ehrman ("Ehrman") and Ehrman Investment Group ("EIG"). Wayne Byles ("Byles") was the original general partner in Onshore. In December of 1984, Byles was succeeded by Roderick Johnson ("Johnson") and EIG as co-general partners. Complaint at 8 ¶ 46; 9 ¶ 49. HPC is an oil and gas operator that had entered an agreement with Onshore to drill wells on certain sites. Complaint at 9 ¶ 49. O'Donnell is the president of HPC and has been sued individually and as president. Complaint at 1.

Unlike many of the oil and gas programs promoted during the early 1980s, Onshore is a program that actually drilled and recovered oil and gas and has made payments to the Plaintiffs. *See* Complaint at 25 ¶ 110. In fact, Onshore continued in operation as of the date summary judgment was granted by the District Court. Plaintiffs are not dissatisfied because Onshore's promoter allegedly stole their money, the general partner is in bankruptcy, or no drilling was ever completed. Instead, Plaintiffs are dissatisfied because their investment strategy to get rich from an investment that looked lucrative in 1984 did not turn out quite as planned. *See, e.g.*, Binder dep. at 45-46. Unfortunately, because of

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1. A final record of this case has not been completed by the District Court. Attorneys for Houston Petroleum Company and Richard O'Donnell have contacted the clerk for the Fifth Circuit and were instructed to cite directly to the pleadings and documents referred to in their brief to this Court.

the inherent risk associated with oil and gas drilling, one of which is the price of oil and gas and the fact that such prices have plummeted since 1984, these programs did not turn out to be as immediately profitable as the Plaintiffs anticipated. Binder dep. at 45-46; Garcia-Quiroga dep. at 98, 101; Steubing dep. at 69-70, 107-08. Therefore, Plaintiffs have simply brought this action claiming a laundry list of fraud and deception to get out of their investments. Complaint at 3-4.

Included among Plaintiffs' allegations are claims against HPC and O'Donnell for alleged violations of the federal and state securities laws, common law fraud and Racketeer Influenced & Corrupt Organization Act ("RICO"). The undisputed evidence establishes that HPC and O'Donnell were not involved in the selling of Plaintiff's limited partnership interests, made no representations, misrepresentations, or omissions of fact to the Plaintiff-investors, and were not involved in any RICO activities. Thus, because there is a lack of evidence to support at least one essential element of each of the Plaintiffs' claims, HPC and O'Donnell are entitled to and were properly granted summary judgment.

SUMMARY OF THE ARGUMENT

The District Court's order granting summary judgment is well reasoned and sound. In their motion for summary judgment and the accompanying evidence, HPC and O'Donnell met the initial burden of production imposed on them by the United States Supreme Court in ***Celotex Corp. v. Catrett***, 477 U.S. 317 (1986). The law does not require the District Court to specifically state in its order that a movant has met his burden of production. In any event, the District Court's order in this case, taken as a whole,

makes it clear that the court found that HPC and O'Donnell met their burden.

Plaintiffs have alleged numerous violations of federal securities laws. Without reaching the merits of these actions, the District Court found that all of Plaintiffs' federal securities laws claims were barred by the applicable statute of limitations. Some of the statute of limitations periods include a discovery rule, and the District Court correctly noted that the Plaintiffs had obtained all of the information necessary to discover any securities law violation by May of 1985, more than two years before Plaintiffs filed suit in December of 1987. Further, Plaintiffs, in their brief to this Court, have raised a claim that the reconfirmation agreements are voidable as untimely; however, this claim is raised for the first time on appeal and therefore should not be considered by this Court. Additionally, this claim, like all the other federal securities law claims, is barred by the statute of limitations.

Even assuming that some or all of Plaintiffs' securities claims are not barred by the statute of limitations, those claims fail due to a lack of some essential element or elements. HPC and O'Donnell were not "sellers" of the partnership units as required by federal securities law but rather they were only the drilling contractor hired by the partnership to drill for oil. At no time did HPC or O'Donnell engage in the sale of Onshore units. HPC and O'Donnell were also not "control" persons under the Securities Act of 1933 because they had no role in the operation or management of the Onshore partnership. Additionally, there is no Rule 10b-5 liability because the record is clear that neither HPC nor O'Donnell ever made any representations to any Plaintiff, and therefore could not make any misrepresentations. Because HPC and O'Donnell were merely the drilling contractor, and were not in a

fiduciary relationship with any Plaintiff, HPC's or O'Donnell's alleged failure to disclose any information which they supposedly had cannot be considered a misrepresentation. Likewise, because Texas case law holds that the elements of a violation of the Texas Securities Act are substantially similar to the elements establishing a violation of Rule 10b-5, Plaintiffs' Texas securities law claim also must fail.

As noted above, because HPC and O'Donnell made no representations and had no duty to disclose, HPC and O'Donnell cannot be held liable for any alleged common law fraud.

Plaintiffs assert that summary judgment is not proper in this case because Defendants, in their pre-trial order, noted the existence of twenty-eight contested issues of fact. Plaintiffs' reliance on this argument is misplaced for two reasons. First, the twenty-eight contested issues of fact listed in the pre-trial order are rendered immaterial for summary judgment purposes. This is true because of the District Court's findings that the various claims fail as a matter of law either because of statute of limitations or because of Plaintiffs' failure to provide sufficient summary judgment evidence on some element essential to their case. Second, a pre-trial order is not proper summary judgment evidence because its purpose -- to narrow the issues to be tried -- is far different from the purpose of a summary judgment, which is designed to allow the court to determine whether the contested issues are both genuine and material.

Finally, HPC and O'Donnell did not violate the federal RICO Act. First, Plaintiffs cannot establish a violation of any of the four sections of the RICO Act necessary for RICO liability. Second, Plaintiffs have presented no evidence to support their allegation that

Onshore is a RICO enterprise. Third, Plaintiffs' minimal allegations of RICO predicate acts fall far short of establishing the "pattern" necessary for RICO liability.

ARGUMENT

I. THE DISTRICT COURT PROPERLY GRANTED SUMMARY JUDGMENT FOR HPC AND O'DONNELL BECAUSE HPC AND O'DONNELL MET THEIR BURDEN ENTITLING THEM TO SUMMARY JUDGMENT AND BECAUSE PLAINTIFFS FAILED TO BRING FORTH SPECIFIC FACTS OR EVIDENCE TO DEFEAT THAT RIGHT.

"Summary judgment is proper if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." FED. R. CIV. P. 56(c). The moving party seeking summary judgment always bears the initial responsibility of informing the district court of the basis for its motion. ***Celotex Corp. v. Catrett***, 477 U.S. 317, 323 (1986). At a minimum, the burden may be discharged by pointing out to the court that there is an absence of evidence to support the nonmoving party's case. ***Celotex***, 477 U.S. at 325. The burden then shifts to the nonmoving party to go beyond the pleadings and designate "specific facts showing that there is a genuine issue of material fact for trial" in order to defeat summary judgment. ***Celotex***, 477 U.S. at 324. HPC and O'Donnell met their burden as the movants. Plaintiffs, in their response to HPC's and O'Donnell's Motion for Summary Judgment, did not designate specific facts showing a genuine issue of material fact. Instead, Plaintiffs responded to HPC's and O'Donnell's motion by merely reasserting allegations

contained in their pleadings and representing to the District Court that they would present evidence at trial supporting these allegations. Plaintiffs failed to show specific facts which tend to contradict HPC's and O'Donnell's proof presented with the motion for summary judgment. Therefore, summary judgment was properly granted for Defendants HPC and O'Donnell.

A. HPC And O'Donnell Met Their Burden Entitling Them To Summary Judgment

HPC and O'Donnell met their initial burden by filing a motion for summary judgment negating Plaintiffs' claims and showing the absence of any genuine issue of material fact. This motion was supported by affidavits, deposition testimony and other evidence obtained through extensive discovery. See HPC and O'Donnell's Motion for Summary Judgment. HPC and O'Donnell specifically set forth their entitlement to summary judgment against the Plaintiffs' claims as follows:

1. Section 12 and 15 claims under Securities Act of 1933
   a. Plaintiffs' Section 12 and 15 claims were barred by the applicable statute of limitations in 15 U.S.C. § 77(m).

   b. HPC and O'Donnell were not "sellers" within the definition provided by the Act.

   c. HPC and O'Donnell were not "control" persons as defined by the Act.

2. Section 10b-5 claims under the Securities Act of 1934

   a. HPC nor O'Donnell made any representations to the Plaintiffs.

   b. HPC nor O'Donnell owed any duty to the Plaintiffs.

3. Claims under the Texas Securities Law

   a. Plaintiffs cannot establish a claim for the same reasons outlined in the preceding section regarding the Plaintiffs' Section 10b-5 claims.

   b. Plaintiffs admitted that neither HPC nor O'Donnell ever made any representations to them.

4. Defendants did not commit common law fraud

5. RICO claims

   a. Plaintiffs lack RICO standing.

   b. RICO enterprise cannot be established.

   c. Pattern of racketeering activity cannot be established.

   d. Plaintiffs cannot establish activities prohibited by RICO.

By providing evidence tending to negate Plaintiffs' claims, HPC and O'Donnell went beyond the minimum requirement to establish a movant's right to summary judgment -- pointing out to the District Court the lack of evidence supporting a nonmoving party's case -- and shifted the burden to the nonmovant Plaintiffs. Plaintiffs' position, "that the Defendants never met their initial burden," is without merit.[2]

B. Plaintiffs Failed To Bring Forth Specific Facts And Evidence Sufficient To Defeat HPC's And O'Donnell's Entitlement To Summary Judgment

After the moving party has met its initial burden, Rule 56(e) requires the nonmoving party to go beyond the pleadings and, by its own affidavits, depositions, answers to interrogatories, and admissions on file, designate specific facts showing that there is a genuine issue for trial. ***Celotex***, 477 U.S. at 324. Plaintiffs attempted to meet this burden by making broad, conclusory allegations with promises of evidence in their possession and proof to be provided at trial.[3] "A party resisting a motion for summary judgment

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2. Throughout Plaintiffs' response to HPC and O'Donnell's Motion for Summary Judgment and Plaintiffs' brief to this Court, they have made accusations against the "Defendants" generally, without identifying which specific Defendant or Defendants of which they are complaining. This is confusing to the Court and the Defendants themselves and requires each Defendant to distinguish itself from all others with respect to a given allegation.

3. Just a few of these excerpts are: "Plaintiffs possess evidence ..."; "At the trial on the merits, Plaintiffs will be able to clearly show..."; "Plaintiffs will be able to show acts..."; "Plaintiffs at a minimum can clearly establish..."; "Plaintiffs contend that the evidence will

must do more than make conclusory allegations, it must set forth specific facts showing that there is a genuine issue for trial." ***Dart Industries, Inc. v. Plunkett Co. of Oklahoma***, 704 F.2d 496, 498 (10th Cir. 1983).

Nowhere in Plaintiffs' response to HPC and O'Donnell's Motion for Summary Judgment do they provide specific facts or evidence showing that a "genuine issue" of "material fact" exists. ***See, e.g., Anderson v. Liberty Lobby, Inc.***, 477 U.S. 242 (1986); ***Matsushita Elec. Indus. Co. v. Zenith Radio Corp.***, 475 U.S. 574 (1986). The only "evidence" Plaintiffs offered, after 18 months of discovery, was an unsigned letter and a one page deposition excerpt from Ms. Joel Middlebrook, the bookkeeper for the partnership.[4] As the District Court correctly stated in its order, the Plaintiffs' response to HPC's and O'Donnell's motion contained "only one exhibit, a rambling, stream of consciousness letter from one Defendant to another which proves nothing." Order at p. 22. In addition, Ms. Middlebrook did not purchase any shares of Onshore and is not a plaintiff in this lawsuit. While the deposition excerpt and the letter do illustrate Ms. Middlebrook's dissatisfaction with HPC, neither of these provide evidence that HPC or O'Donnell are, or may be, guilty of possible securities act or RICO violations but only amount to mere supposition and speculation. To the contrary, the evidence clearly shows that HPC and O'Donnell made no representations, misrepresentations, omissions of fact, or had any connection whatsoever with the sale or purchase of the Onshore units. Therefore, Plaintiffs simply defaulted on their obligation to bring forth

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establish..."; "Plaintiffs will show at trial..."; "Plaintiffs contend that they will be able to prove..."

4. Ms. Middlebrook had no connection with the sale or purchase of Onshore units.

specific facts and evidence raising a genuine issue of material fact. Because HPC and O'Donnell met their burden to show their right to summary judgment, and because Plaintiffs wholly failed to bring forth specific facts or evidence sufficient to defeat that entitlement, the District Court properly granted summary judgment for HPC and O'Donnell.

C. Plaintiffs Are Not Entitled To Assert Or Present Alleged New Evidence Or Allegations For The First Time On Appeal From The Granting Of The Summary Judgment For HPC And O'Donnell.

A party appealing the granting of a summary judgment motion cannot bring forth new evidence or allegations beyond those presented to the trial court. ***Frank C. Bailey Enterprises, Inc. v. Cargill, Inc.***, 582 F.2d 333, 334 (5th Cir. 1978). On appeal, Plaintiffs are limited to the allegations and exhibits they presented to the District Court in their response to HPC and O'Donnell's summary judgment motion. Plaintiffs' brief is full of assertions and alleged evidence which was not presented to the District Court and should not be considered by this Court.[5] The Plaintiffs do not get a second chance to bring forth alleged new evidence

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5. Examples of new evidence and allegations made by the Plaintiffs for the first time are: (1) Defendants Joint Pretrial Order recognizes 28 contested issues of material fact; Plaintiffs' brief at 37. (2) Plaintiffs are entitled to avoid the reconfirmation contracts because they were "made" in violation of SEC "rules"; Plaintiffs' brief at 39 and 40. (3) Defendants' authorization of secondary sales of securities, in complete violation of Rule 502(d) of Regulation D, resulted in a continuous offering to the public for an indefinite period; Plaintiffs' brief at 45. (4) Plaintiffs are entitled to summary judgment ... since the Defendants gained Plaintiffs' reconfirmation acceptances in violation of the law. Plaintiffs' brief at 50.

for the first time on appeal in an attempt to raise a genuine issue of material fact.

Additionally, before addressing Plaintiffs' arguments concerning alleged securities violations regarding the sale of the Onshore units, the relationship between Plaintiffs and HPC and O'Donnell needs to be specifically noted. All of Plaintiffs' allegations of securities violations concern representations made to them in the sale of the Onshore units. Neither HPC nor O'Donnell were directly or indirectly involved in the sale of Onshore units to any of the Plaintiffs. HPC is an oil and gas operator that entered into an agreement with Onshore to drill prospective oil and gas wells. However, HPC and O'Donnell are forced to address each of the securities allegations because of the all-inclusive nature of Plaintiffs' charges. In this regard, the essential fact that HPC and O'Donnell's only involvement with the Plaintiffs was that of a drilling contractor for the Onshore partnership should not be overlooked.

II. THE DISTRICT COURT PROPERLY GRANTED SUMMARY JUDGMENT FOR HPC AND O'DONNELL BECAUSE PLAINTIFFS' SECTION 12(1) AND 12(2) CLAIMS ARE BARRED BY STATUTE OF LIMITATIONS

Plaintiffs allege that the Defendants violated Sections 12(1) and 12(2) of the Securities Act of 1933. Section 13 of the 1933 Act provides a clear statute of limitations for these sections:

> "No action shall be maintained to enforce any liability created under section 77k or 77l(2) [section 12 (2)], of this title unless brought within one year after the discovery of the

> untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or if the action is to enforce a liability created under section 77l(1) [section 12(1)], of this title, unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under . . . section 77l [section 12(2)] more than three years after the sale."

15 U.S.C. § 77m (1982). The District Court correctly found that both of these claims are barred by the statute of limitations.

A. Plaintiffs' Section 12(1) Claims

Plaintiffs have alleged that the sale of the Onshore units violated Section 12(1) of the Securities Act of 1933, 15 U.S.C. § 77l(1). This section creates civil liability where mail and other instrumentalities of interstate commerce are used in the sale, delivery, or offer of sale of an unregistered security, as prohibited by Section 5 of the 1933 Act, 15 U.S.C. § 77e. The 1933 Act imposes a requirement of timeliness in prosecuting a Section 12(1) cause of action. It states in pertinent part: "No action shall be maintained ... to enforce a liability created under ... 77l(1) of this title, unless brought within one year after the violation upon which it is based." 15 U.S.C. § 77m (1982).

In determining when the statute of limitations begins to run, the relevant inquiry is to determine which of a defendant's activities--offer, sale, or delivery of the security--occurred last. ***Doran v. Petroleum Management Corp.***, 576 F.2d 91, 93 (5th Cir. 1978). The limitations period begins to run upon the last action of the defendant. ***Doran***, at 93. The last action in the sale of the Onshore units was the

reconfirmation offer sent to the Plaintiffs in January of 1985. Therefore, the one-year statute of limitation established by 15 U.S.C. § 77m for any violation of Section 12(1) would have begun to run in January 1985. The latest date that any of the Plaintiffs could have filed suit in order to toll the applicable limitation period would have been in January of 1986. The Plaintiffs did not file suit until December 3, 1987, well beyond the applicable limitations period. Thus, Plaintiffs' claims for alleged violations under Section 12(1) are time-barred.

B. Plaintiffs' Section 12(2) Claims

Section 12(2) of the Securities Act imposes liability on any person who offers or sells a security by means of:

> [A] prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading. . . .

15 U.S.C. § 77l(2). Plaintiffs' Section 12(2) claims are based upon allegations that Defendants lured them into purchasing Onshore units by "general solicitations", "dog-and-pony shows" and "puffery". In essence, Plaintiffs argument is that they were assured by the Defendants that this was a sound and lucrative venture. However, each Plaintiff signed a subscription agreement with their initial purchase of Onshore units. The subscription agreement set forth the risks, warned about possible losses, and put the investor on notice of the speculative nature of their investment.

The subscription agreement's pertinent parts read as follows:

> 3.(a) **[The Investor warrants that he] (i) has adequate means of providing for his current needs ... and he has no need for liquidity of his investment ... (ii) with respect to each one (1) Unit subscribed, (1) has a net worth of at least $200,000 ... and can bear the economic risk of losing his entire investment herein, and (iii) has ... such knowledge and experience in financial matters that he is capable of evaluating the relative risks and merits of this investment.**
>
> 3.(d) **He has received and read or reviewed ... and is familiar with, the Partnership Agreement, the Memorandum, and this Agreement ...**
>
> 3.(l) **That the Partnership has no significant financial or operating history**; this is the Partnership's first venture and the Units are speculative investments which involve a high degree of risk of loss by him of his entire investment in the Partnership.
>
> 4. **The following representations, guarantees or warranties have never been made to him by the General Partners, its agents, or employees or any other person, expressly or by implication:**
>
> (ii) **The percentage of profit and /or amount of or type of consideration, profit**

> **or loss ... to be realized, if any, as a result of this investment.**
>
> (iii) **The past performance or experience on the part of the General Partners or any of its affiliates,** any securities broker of finder, their partners, salesmen, associates, agents, or employees or of any other person, will in any way, indicate or predict the results of the ownership of Units or of the overall Partnership venture.
>
> 11. **The undersigned specifically acknowledges that he/she understands that Houston Petroleum is not a General Partner in this program**. W. Roderick Johnson is the Managing General Partner and Ehrman Investment Group, Inc. is Co-General Partner of Onshore Exploration Ltd. 1984 Mid-Year. No other representations to the contrary have been implied or expressed.

Assuming Plaintiffs' allegations of misrepresentations are true, the subscription agreement put Plaintiffs on notice of possible discrepancies between what they were being told and what the subscription agreement provided. This triggered the duty to exercise reasonable diligence. ***Kennedy v. Josephthal & Co. Inc.***, 814 F.2d 798 (1st Cir. 1987). Therefore, the statute of limitations under the 1933 Act began to run when each Plaintiff had the opportunity to examine the subscription agreement.

This same issue was decided by the First Circuit in ***Kennedy v. Josephthal & Company, Inc.***, 814 F.2d 798 (1st Cir. 1987). In ***Kennedy***, glaring differences between terms

of an offering memorandum and statements made to prospective investors placed those investors on inquiry notice at the time they had an opportunity to examine the offering memorandum in light of oral representations. ***Kennedy*** at 802. The First Circuit found, as a matter of law, the exercise of reasonable diligence would require more from a party than merely viewing two sets of statements, one of which logically cannot be true, and choosing one of those sets. ***Kennedy***, 814 F.2d 803.

This lawsuit was filed on December 3, 1987. All of the Plaintiffs, except Steubling, LaCelle, Mikles and MJM, purchased their Onshore units before November 30, 1984, by executing the subscription agreement. Therefore, under the discovery rule of Section 77m, the latest date that any of the included Plaintiffs could have filed suit in order to toll the one-year limitation period would have been December 1, 1985. Disregarding the discovery rule of Section 77m, the latest date that these Plaintiffs could have filed suit to toll the three-year limitation period would have been December 1, 1987. In either instance, their claims are barred by both the one-year and three-year limitation periods in 15 U.S.C. § 77m. The remaining Plaintiffs purchased their Onshore units and executed the subscription agreement by May 1, 1985. Thus, these claims are barred by the one-year statute in 15 U.S.C. § 77m. (1982).

III. THE DISTRICT COURT PROPERLY GRANTED SUMMARY JUDGMENT FOR HPC AND O'DONNELL BECAUSE PLAINTIFFS' 10b-5 CLAIMS ARE BARRED BY THE STATUTE OF LIMITATIONS

Plaintiffs allege various violations of Section 10(b) of the Exchange Act of 1934 and Rule 10b-5. Section 10(b) provides for an action by a purchaser or seller of "any

security" against "any person" who used "any manipulative or deceptive device or contrivance" in the purchase or sale of a security. 15 U.S.C. § 78(j)(b) (1982). The essential elements of a Section 10(b) and Rule 10b-5 claim are: (1) in a securities transaction (2) the defendants acting with scienter (3) made a material misrepresentation or nondisclosure (4) upon which plaintiff relied, and (5) thereby suffered injury. ***Chemetron Corp. v. Business Funds, Inc.***, 718 F.2d 725, 728 (5th Cir.), *vacated on other grounds*, 460 U.S. 1007(1983).

This Court in ***Wood v. Combustion Engineering Inc.***, 643 F.2d 339, 341 (5th Cir. 1981), determined that the appropriate limitations period for 10b-5 claims in Texas was two years. The limitations period begins to run when the plaintiff discovers, or in the exercise of reasonable diligence should discover, the alleged violations. ***Corwin v. Marney, Orton Investments***, 788 F.2d 1063 (5th Cir. 1986). By exercising reasonable diligence, the Plaintiffs should have been put on notice of any alleged misrepresentations made concerning the Onshore units when they read and executed the subscription agreement.

As noted previously, the subscription agreement was clear and concise in its warnings of the risks involved, experience of the general partners, and the possibility that all of a subscriber's investment might be lost. Any oral representations made to the Plaintiffs which was not consistent with the language of the subscription agreement put them on notice and started the limitations period running. All Plaintiffs had executed the subscription agreement by May 1, 1985. The latest date that the Plaintiffs could have filed suit asserting a claim under Section 10(b) and Rule 10b-5 would have been May 2, 1987. The present lawsuit was not filed until December 3, 1987. Therefore, under the two -year limitations period to assert a 10b-5 claim, as

determined by this Court in ***Wood***, Plaintiffs' claims under 10b-5 are also time-barred.

IV. PLAINTIFFS' ASSERTIONS THAT THE RECONFIRMATION AGREEMENTS WERE UNTIMELY AND THUS ARE VOIDABLE CANNOT DEFEAT SUMMARY JUDGMENT BECAUSE THE CLAIM WAS NOT PRESERVED FOR APPEAL. THESE ASSERTIONS ARE ALSO BARRED BY LIMITATIONS.

In their brief, Plaintiffs have raised a claim that the reconfirmation agreements for the sale of the units are voidable because they were signed after the all-or-none offering had expired. This claim is not valid for two reasons.

First, Plaintiffs have raised this issue for the very first time on appeal to this Court. Nowhere in their First Amended Complaint did Plaintiffs allege facts establishing a right to void the agreements on this basis. Further, the issue was not addressed in HPC and O'Donnell's Motion for Summary Judgment, the Plaintiffs' response to HPC and O'Donnell's Motion for Summary Judgment, nor the District Court's order granting summary judgment to HPC and O'Donnell. Plaintiffs cannot avoid summary judgment by untimely raising an issue never before presented to the District Court nor to Defendants. ***Frank C. Bailey Enterprises, Inc. v. Cargill, Inc.***, 582 F.2d 333, 334 (5th Cir. 1978)

Second, even assuming that this claim had been plead at a proper time and place, and further assuming that the allegations are all true, Plaintiffs' claim is time-barred under the same statute which provides the right they assert. *See*

Securities Exchange Act of 1934, § 29(b), 15 U.S.C. § 78cc(b) (1982). This section provides that:

> No contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, . . .unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

Id. (emphasis added). Plaintiffs acknowledge in their brief that these reconfirmation agreements were entered into in January, 1985. Accordingly, Plaintiffs should have known that the reconfirmation agreements were made after the expiration of the all-or-none offering at the time they signed those agreements in January of 1985. Plaintiffs did not bring suit until December 3, 1987, more than two years after this discovery in January, 1985, that the reconfirmation agreements were in violation of the Securities Act, and long after the one-year deadline for filing suit had expired.

Because Plaintiffs have raised this claim for the first time on appeal and because this claim is also time-barred, Plaintiffs' assertions regarding the untimeliness of the reconfirmation agreements cannot constitute a ground for reversal of the District Court's summary judgment order.

V. THE "20 CONTESTED ISSUES OF FACT" IN DEFENDANTS' PRE-TRIAL ORDER WERE NOT MATERIAL AND THUS ARE IRRELEVANT TO THE DISTRICT COURT'S SUMMARY JUDGMENT ORDER.

In Plaintiffs' brief, much is made of the fact that, following Defendants' motions for summary judgment, all

Defendants filed a joint pretrial order which included a list of 20 contested issues of fact.[6] See Plaintiffs' Brief at 35-36. This point is irrelevant for two reasons.

First, while Plaintiffs characterize the list in the joint pretrial order as a list of "twenty contested issues of material fact" (Plaintiffs' Brief at 36), the list is not one of "material facts" as that term is used in the summary judgment context. The Supreme Court has clearly defined materiality: "[A] complete failure of proof concerning an essential element of the non-moving parties case necessarily renders all other facts immaterial." ***Celotex,*** 477 U.S. at 323. Similarly in ***Anderson v. Liberty Lobby, Inc.***, 477 U.S. 242, the Supreme Court stated that "[o]nly disputes or facts that might affect the outcome of the suit under the governing law will properly preclude the entry of summary judgment. Factual disputes that are irrelevant or unnecessary will not be counted." ***Id.*** at 248. Therefore, where, as here, the summary judgment evidence establishes that one of the elements of the Plaintiffs' cause of action does not exist as a matter of law, or that Plaintiffs' cause of action is barred by a statute of limitations, all other contested issues of fact are rendered immaterial.[7]

Second, a pretrial order is not listed in Rule 56(c) as proper summary judgment evidence. This is for a good reason.

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6. Plaintiffs argue that Defendant Rockwood Insurance Company ("Rockwood") listed "an additional 8 contested issues of fact." Plaintiffs' Brief at 12-13. However, for purposes of the above analysis, the discussion will be restricted to those allegations that are relevant only to HPC and O'Donnell.

7. It should also be noted that the District Court granted summary judgment after the pre-trial order containing the "twenty contested issues of fact" was presented to the Court.

> The functions of the pretrial conference described in Rule 16 and the summary judgment motion provided in Rule 56 . . . are entirely different. . . .Upon a proper showing that there is no genuine issue to be tried, a judge may grant a motion for summary judgment wholly irrespective of the terms of a pretrial order specifying a number of issues which remained after the discussion at the pretrial conference had eliminated others.

Irving Trust Company v. United States, 221 F.2d 303, 305 (2d Cir.), *cert. denied*, 350 U.S. 828 (1955). In short, the purpose of a pretrial order is to narrow the issues to be tried while the purpose of a summary judgment is to determine whether those issues are both genuine and material. The fact that all Defendants in this case noted 20 contested issues of fact in the pre-trial order does not prevent the District Court's subsequent determination that those issues were not material to the outcome of the case.

The preceding arguments, considered alone, are sufficient to uphold the District Court's order granting HPC and O'Donnell's Motion for Summary Judgment. However, recognizing that this Court's review of the District Court's summary judgment order is *de novo*, Defendants HPC and O'Donnell summarize additional arguments that were presented to the District Court in their motion for summary judgment. These arguments, while not reached by the District Court, provide ample grounds for sustaining the granting of summary judgment.

VI. HPC AND O'DONNELL DID NOT VIOLATE ANY PROVISION OF THE SECURITIES ACT OF 1933

Plaintiffs' allegations under Sections 12 and 15 seek to impose liability on HPC and O'Donnell for alleged oral and written misrepresentations in connection with the offer and sale of the Onshore partnership units. Recent Supreme Court and Fifth Circuit precedent conclusively demonstrates that liability for any alleged violations of the Securities Act of 1933 cannot be imposed against HPC or O'Donnell because they do not meet the statutory definition of a "seller" under the Act.

A. Elements Required to Establish Section 12 and 15 Claims

Plaintiffs' Complaint contains vague, confusing and essentially meaningless cross-references that attempt to assert a cause of action against HPC and O'Donnell under Sections 12 and 15 of the Securities Act of 1933, 15 U.S.C. § 77(l), (o) (1982). Complaint at 29, 34 and 39. Section 12(1) provides a cause of action against anyone who offers or sells a security in violation of § 77(e) which makes it unlawful to use interstate commerce as the means to sell a security unless a registration statement is in effect and the prospectus meets the requirement of the Act. 15 U.S.C. § 77(l)(1). Section 12(2) provides a private cause of action against any person who offers or sells a security through communications which include material misrepresentations or omissions of material facts. ***Id.*** § 77(l)(2). Section 15 provides a private cause of action against any person who controls any person liable under Sections 12(1) or 12(2). ***Id.*** § 77(o). To come within the ambit of these statutory provisions, Plaintiffs must have had to establish that HPC and O'Donnell were "sellers" of their securities.

B. HPC and O'Donnell are not "Sellers"

The Supreme Court redefined persons liable under Section 12(1) of the Securities and Exchange Act of 1933 in the case of ***Pinter v. Dahl***, 486 U.S. 622 (1988), finding that the proper inquiry is into the relationship between the investor and the defendant; not the defendant and the transaction. ***Id***. at 2080-81. In directing this inquiry, the Supreme Court specifically held that Section 12(1) "imposes liability on the owner who passed title, or other interest in the security, to the buyer for value," as well as one who "engages in solicitation." ***Id***. at 2076. This Court, following ***Pinter's*** guidance, extended that definition of "seller" to cover claims asserted under Section 12(2) of the Act in the case of ***Abell v. Potomac Insurance Company***, 858 F.2d 1104 (5th Cir. 1988). In ***Abell***, this Court held that when a court examines any claim under Section 12, two inquiries must be made: "(1) [w]ho passed title to the plaintiff or solicited the transaction in which title passed; and (2) from whom did the plaintiff buy the security?" ***Id***. at 1114.

Every case citing to and following ***Pinter*** has expressly declared that a plaintiff must demonstrate that each defendant "actually solicited their investment" for Section 12 liability to attach. *See, e.g.*, ***Capri v. Murphy***, 856 F.2d 473, 479 (2d Cir. 1988) (noting that Second Circuit precedent previously held that the language of Sections 12(1) and 12(2) is identical); accord ***Schlifke v. Seafirst Corp.***, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174 (7th Cir. Jan. 9, 1989) (holding that a bank that financed allegedly illegal oil and gas limited partnerships was not a "seller" since it did not actively participate in the solicitation of investors or engage in preparing the prospectus except for drafting the loan documents included therein); ***Harelson v. Miller Fin. Corp.***, 854 F.2d 1141, 1142 (9th Cir.), *cert. denied*, 109

S. Ct. 274 (1988) (finding that salesman/agent of defendant corporation "solicited" sales of securities by presenting facts necessary to effectuate sale to purchaser and receiving compensation for bringing sale about); ***In re Professional Fin. Management, Ltd.***, 692 F. Supp. 1057, 1064 (D. Minn. 1988) ("Under the ***Pinter*** standard, liability may be imposed against [defendants] if they were principals to the sale or otherwise assisted in the transfer of securities as brokers, and received financial benefit in return.").

Plaintiffs muster no support for a finding that either HPC or O'Donnell could be declared a "seller" under this standard. The record is clear that neither HPC nor O'Donnell in any way "passed title or other interest" to any Plaintiff. Like the bank in ***Schlifke***, neither HPC or O'Donnell were involved in the solicitation or sale of these interests. *See* O'Donnell Affidavit, attached to HPC and O'Donnell's Motion for Summary Judgment. In fact, the Plaintiffs admitted in deposition that neither HPC nor O'Donnell took part or had any connection in the sale of Onshore units to them. Garcia-Quiroga dep. at 136; Boyett dep. at 86-87; Burroughs dep. at 22-23; McDonald dep. at 1066; Topalian dep. at 127; Steubing dep. at 151; LaCelle dep. at 144, 150, 156-57.

HPC was simply the drilling operator. The undisputed evidence establishes that HPC and O'Donnell were not involved in Onshore's selling efforts. HPC and O'Donnell had no contact with Onshore's sales personnel. *See* O'Donnell's Affidavit. Likewise, there is no evidence to support the allegation that HPC and O'Donnell participated in the preparation of the prospectus or in any way promoted the program. Moreover, the record directly refutes the contention that anyone at HPC had any knowledge of Ehrman's sales tactics. *See* O'Donnell Affidavit. To the contrary, the evidence clearly establishes the opposite:

O'Donnell testified that no HPC personnel had any knowledge of or control over the means by which Ehrman or the Onshore salesmen marketed the limited partnership interests. Boyett dep. at 109; Garcia-Quiroga dep. at 159-60; Burroughs at 84-85; Steubing dep. at 166; Topalian dep. at 135-36; McDonald dep. at 1061; LaCelle dep. at 147-48.

Every passage of record testimony in this case refutes the assertion that HPC and O'Donnell engaged in the direction of or solicitation by Onshore's sales force. HPC and O'Donnell were not engaged in soliciting sales and therefore cannot be said to have been "sellers" of these interests for purposes of the 1933 Act. Plaintiffs' claims pursuant to the 1933 Act were properly dismissed and summary judgment granted.

C. HPC and O'Donnell are not "Control" Persons Under the 1933 Act

HPC and O'Donnell's total lack of control removes any possibility of liability under either the primary, secondary, or "control person" provisions of the 1933 Act. Particularly instructive here is the new decision by the Seventh Circuit in ***Schlifke v. Seafirst Corp.***, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174, at 91,592 (7th Cir. Jan. 9, 1989). In deciding that liability under the 1933 Act could not lie against defendant Seafirst, the court noted that:

> Although the Bank necessarily became involved in the transaction . . . to the extent necessary to fully document and protect its loans and collateral, there is no evidence that [it] thereby intended to be making an investment or that it took any steps to induce any investment by [the borrower] with [the seller].

> Thus, we agree with the district court that the Bank was acting merely as a commercial lender when it extended a loan to ENI 1981-III at a fixed rate of interest.

Id. at 91,597 (citations omitted, ellipses in original).

The *Schlifke* court expressly refused to allow any cause of action based on "aiding and abetting" liability under Section 12(2). *Id.* at 91,597-98. Likewise, in the recent decision of *Commins v. Johnson & Higgins, Inc.*, 1988 Fed. Sec. L. Rep. ¶ 94,092 (N.D. Cal. Sept. 28, 1988), the court explained that "control person" liability imposes liability "only on a person who 'stands behind the scenes and controls the [securities violator] who is in a nominal position of authority.'" *Id.* at 91,099 (quoting *Wool v. Tandem Computers, Inc.*, 818 F.2d 1433, 1441 (9th Cir. 1987)).

The record specifically negates any contention that HPC or O'Donnell played any part in the operation or management of Onshore. *See* O'Donnell Affidavit; Boyett dep. at 109; Garcia-Quiroga dep. at 159-60; Burroughs dep. at 84-85; Steubing dep. at 166; Topalian dep. at 135-36; McDonald dep. at 1061; LaCelle dep. at 147-48. The evidence clearly shows that no HPC employee or officer directed or controlled any of the policies, management, decisions, people, or any other aspects of the business of Onshore, including any sales effort. *See* O'Donnell Affidavit.

Thus, both the record testimony and the applicable legal principles make it clear that HPC and O'Donnell played no role in the operation of Onshore, in the sale of the Onshore units, or in the solicitation of Plaintiffs' investment interests. HPC and O'Donnell did not direct or control any Onshore employee or operation. As such, HPC was merely

the drilling operator for some of the wells and cannot be found liable under the provisions of the 1933 Act.

VI. HPC AND O'DONNELL DID NOT VIOLATE ANY PROVISIONS OF THE SECURITIES ACT of 1934

Plaintiffs additionally assert that HPC and O'Donnell violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. Plaintiffs cannot recover under either theory because HPC and O'Donnell made no misrepresentation to Plaintiffs, and owed no duty to disclose and therefore made no omission of fact.

A. Elements Required to Establish Section 10(b) and Rule 10b-5 Claims

Plaintiffs allege various violations of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. Section 10(b) provides an action by a purchaser or seller of "any security" against "any person" who used "any manipulative or deceptive device or contrivance" in connection with the purchase or sale of a security. 15 U.S.C. § 78(j)(b) (1982). The essential elements of a Section 10(b) and Rule 10b-5 claim are (1) in connection with a securities transaction and (2) acting with scienter, the defendants made (3) a material misrepresentation or nondisclosure (4) upon which plaintiff relied and (5) thereby suffered injury. ***Chemetron Corp. v. Business Funds, Inc.***, 718 F.2d 725, 728 (5th Cir.), *vacated on other grounds*, 460 U.S. 1007 (1983); ***Pin v. Texaco, Inc.***, 1986 Fed. Sec. L. Rep. (CCH) ¶ 92,823, at 94,011 (5th Cir., July 14, 1986).

Most significantly, the Plaintiffs must prove that "the defendant(s) acted with scienter, *i.e.*, with intent to deceive,

manipulate, or defraud."[8] ***Herman & MacLean v. Huddleston***, 459 U.S. 375, 382 (1983). As the Supreme Court put it, "Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud." ***Chiarella v. United States***, 445 U.S. 222, 234-35 (1980). No Plaintiff has yet to or can now point to any fact in support of their allegation that HPC or O'Donnell were guilty of fraud. Burroughs dep. at 84-85; Garcia-Quiroga dep. at 159-60; Boyett dep. at 107-09, 111; LaCelle dep. at 161-62, 183; Steubing dep. at 165-67; Topalian dep. at 135-36; McDonald dep. at 1079. Accordingly, Plaintiffs cannot establish an essential element of their 1934 Act claim.

B. HPC and O'Donnell Made No Representation to Plaintiffs

To recover under Rule 10b-5, Plaintiffs must establish that HPC or O'Donnell made a misrepresentation of material fact to the Plaintiffs in connection with the Plaintiffs' purchase of the Onshore units. ***Abell v. Potomac Ins. Co.***, 858 F.2d 1104, 1115 (5th Cir. 1988). Plaintiffs cannot recover from HPC or O'Donnell for any alleged misrepresentation since the uncontroverted testimony of the Plaintiffs establishes that neither HPC nor O'Donnell made any statements, much less untrue statements, to the Plaintiffs. McDonald dep., Vol. VI at 1062-66; Topalian dep. at 151; Garcia-Quiroga dep. at 159; Law dep. at 76; Burroughs dep. at 84-85; LaCelle dep. at 157-163, 168-69. The absence of

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8. In ***Ernst & Ernst v. Hochfelder***, 425 U.S. 185, 203 (1976), the Supreme Court refused to impose a negligence or "should have known" standard into § 10(b) or Rule 10(b)-5 actions. The scienter requirement can be satisfied with a state of mind less than actual knowledge such as "sever recklessness." This standard requires a showing that the deception was "so obvious that the defendant must have been aware of it." ***Warren v. Reserve Fund, Inc.***, 728 F.2d 741, 745 & n.12 (5th Cir. 1984).

any statements is exemplified by Plaintiff Bobby W. McDonald's deposition testimony:

> Q. Do you have any information or evidence to indicate that Richard O'Donnell or HPC made any false representations to anybody to get them to buy Onshore units?
>
> A. No, sir.

McDonald dep. Vol. VI, at 1066. As a further example, Plaintiff Charles F. LaCelle is unequivocal in his answers:

> Q. Do you have any facts that would show that HPC made any representations to you at all?
>
> A. Directly?
>
> Q. Directly or indirectly.
>
> A. No.
>
> Q. What about Mr. O'Donnell? Did he make any representations to you?
>
> A. No.
>
> Q. Would you have -- do you have any facts, or are you aware of any facts, that would show that HPC or Mr. O'Donnell assisted in any fraudulent misrepresentations that others may have made to you?

A. No.

LaCelle dep. at 161-62.

The failure of the Plaintiffs to provide the District Court with any evidence of an untrue statement of material fact by HPC or O'Donnell required that Plaintiffs' 10b-5 claims be dismissed. *See* ***Abell***, 858 F.2d at 1115-16. As such, summary judgment for HPC and O'Donnell on these claims was likewise proper.

C. HPC and O'Donnell Owed No Duty to Plaintiffs

The failure of a party to disclose facts constitutes actionable fraud only if the party had a duty to disclose the facts. ***Chiarella v. United States***, 445 U.S. 222, 230 (1980); ***Tempo Tamers, Inc. v. Crow-Houston Four, Ltd.***, 715 S.W.2d 658, 669 (Tex. App.--Dallas 1986, writ ref'd n.r.e.). Accordingly, the first step in analyzing Plaintiffs' nondisclosure claims is to determine whether HPC or O'Donnell had a duty to disclose facts to Plaintiffs.

First, as drilling operator, HPC and O'Donnell owed no fiduciary duty to the Plaintiffs. A fiduciary relationship generally arises only from a relationship of trust and confidence. ***Thigpen v. Locke***, 363 S.W.2d 247, 252-53 (Tex. 1962). A fiduciary relationship may be created from a variety of circumstances usually involving attorney-client, parent-child or some other special relationship; but generally it does not include relationships between businessmen dealing at arms length. ***Consolidated Gas & Equip. Co. v. Thompson***, 405 S.W.2d 333, 336-37 (Tex. 1966). To allow the Plaintiff investors to transform this arms length transaction between the drilling operator and the Onshore

partnership into a fiduciary duty between the operator and Plaintiffs would jeopardize the security of contracts in Texas. See ***Thigpen***, 363 S.W.2d at 253. Thus, HPC and O'Donnell had no duty to disclose based upon a fiduciary duty.

Moreover, any action by HPC to assure itself of the viability of these programs for which it was about to act as drilling operator lends no support to the conclusion of the Plaintiffs that HPC or O'Donnell owed Plaintiffs a duty to disclose facts regarding their Onshore investments. *See* ***Schlifke***, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174, at 91,599. As one court has noted, it is ludicrous to contend that actions taken by a party in assessing its own risks in connection with a proposed transaction somehow translate into an affirmative duty to advise other participants in the transaction with regard to their decision whether or not to participate. *See* ***National Union Fire Ins. Co. v. Eaton***, 701 F. Supp. 1031 (S.D.N.Y. 1988). In ***Eaton***, the court found that the surety's review of the private placement memoranda for its own purposes did not require it to disclose any information to the investors. *Id.* The court noted that a surety has no duty to disclose adverse information it may have had. *See generally* ***Delany v. Blunt, Ellis & Loewi***, 631 F. Supp. 175 (N.D. Ill. 1986) (citing ***Woodward v. Metro Bank***, 522 F.2d 84 (5th Cir. 1975)); ***Quintel Corp., N.V. v. Citibank, N.A.***, 589 F. Supp. 1235 (S.D.N.Y. 1984); ***Schlifke v. Seafirst Corp.***, 1987 Fed. Sec. L. Rep. (CCH) ¶ 93,107, at 95,443 (N.D. Ill. 1987), *aff'd* 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,174 (7th Cir. Jan. 9, 1989); ***In re Gap Stores Sec. Litig.***, 457 F. Supp. 1135 (N.D. Cal. 1978); ***Ingenito v. Bermec Corp.***, 441 F. Supp. 525, 549 (S.D.N.Y. 1977).

Plaintiffs also assert that even if HPC and O'Donnell were not engaging in primary fraud, they may have aided

and abetted the primary fraud allegedly perpetrated by other Defendants. Under Fifth Circuit precedent, parties are subject to liability for aiding and abetting a securities violation only if the following elements are proven: (1) there must have been a security violation by the primary party; (2) the aider and the abetter must have had a "general awareness" of its role in a Rule 10b-5 violation; (3) the aider and abetter must have knowingly rendered "substantial assistance" in the Rule 10b-5 violation. ***Abell***, 858 F.2d at 1126; *accord* ***Bane v. Sigmundr Exploration Corp.***, 848 F.2d 579 (5th Cir. 1988); ***Woodward v. Metro Bank***, 522 F.2d 84 (5th Cir. 1975).

To establish the "general awareness" element, Plaintiffs must prove that HPC or O'Donnell had knowledge of their role in a fraud and their commitment (or intent) to aid in the fraud's success:

> Scienter, then would require first that the alleged abettor know of the fraud's existence and generally understand how its actions aid in promoting the success of the fraud. The second element of scienter-commitment would be met where evidence shows that the abettor acts from a desire to help the fraud succeed . . .
>
> If the evidence shows no more than a transaction constituting the daily grist of the mill, we would be loathe to find 10b-5 liability without clear proof of intent to violate the securities laws.

Abell, 858 F.2d at 1127, (citing ***Woodward***, 522 F.2d at 97) (emphasis added).

HPC and O'Donnell played no role in the offering of the securities. *See* O'Donnell Affidavit. HPC was simply the drilling operator in this venture. Neither HPC nor O'Donnell knew of the existence of any alleged fraud nor intended to help such alleged fraud succeed. *See* O'Donnell Affidavit. All of their actions were "daily grist of the mill" actions of a drilling operator.

Similarly, Plaintiffs cannot establish that HPC or O'Donnell "substantially assisted" in the alleged fraud. *See* ***Bane***, 848 F.2d at 581. In ***Bane***, the defendant was a lender who included loan documents in an investment package for an oil and gas limited partnership and made loans to some of the plaintiffs. ***Id***. at 580. The court held that the inclusion of documents in investor packages and loaning money to the investors did not constitute "substantial assistance" for purposes of imposing liability on the lender for aiding and abetting in the securities violation under Rule 10b-5. ***Id***. at 581.

In this case, HPC acted solely as the drilling operator. Thus, HPC was even more removed from the Plaintiffs' investments than the surety, lender or escrow agent in ***Eaton***, ***Schlifke*** and ***Bane***. HPC did not review the investors' financial information and did not even know their identity until this lawsuit was filed. *See* O'Donnell Affidavit. HPC had no contact or communication in even the most remote sense with any of the investors prior to their investment. *See* O'Donnell Affidavit. HPC did not contribute to the prospectus. *See* O'Donnell Affidavit. As in ***Bane***, although a copy of the agreement between Onshore and HPC was attached to the prospectus, this is not sufficient to establish "substantial assistance." Plaintiffs even admit in their Complaint that HPC's limited role was fully disclosed in the prospectus. Complaint at 12-14. Plaintiffs have no basis for asserting that HPC or O'Donnell had any duty to disclose.

Therefore, there exists no basis for imposing liability on HPC or O'Donnell under Section 10(b) and Rule 10b-5. Accordingly, the Plaintiffs' allegations regarding these causes of action were appropriately dismissed by the District Court and the court's granting of the summary judgment was proper.

VII. HPC AND O'DONNELL DID NOT VIOLATE THE TEXAS SECURITIES LAW

Plaintiffs allege generally that HPC and O'Donnell's actions violated the Texas Blue Sky Securities Act. TEX. REV. CIV. STAT. ANN. art. 581-33 (Vernon Supp. 1989). The elements necessary to establish a violation of the Texas Securities Act are substantially similar to those necessary to establish a violation of Rule 10b-5. Thus, a failure to prove a violation of Rule 10b-5 generally is considered a failure to prove a Texas Securities Act violation. *See* ***Keasler v. Natural Gas Pipeline Co. of Am.***, 569 F. Supp. 1180 (E.D. Tex. 1983), *aff'd*, 741 F.2d 1380 (5th Cir. 1984); ***Jeanes v. Henderson***, 688 S.W.2d 100 (Tex. 1985); ***Sibley v. Horn Advertising, Inc.***, 505 S.W.2d 417 (Tex. Civ. App.--Dallas 1974, writ ref'd n.r.e), *cert. denied*, 420 U.S. 929 (1975). For the same reasons that Plaintiffs cannot establish that HPC or O'Donnell violated Rule 10b-5, they likewise cannot establish a violation of the Texas Blue Sky Securities. Therefore, the District Court was correct in dismissing these claims and granting the summary judgment for HPC and O'Donnell.

VIII. HPC AND O'DONNELL DID NOT COMMIT COMMON LAW FRAUD

Plaintiffs have no cause of action against HPC or O'Donnell on a theory of common law fraud. The elements of actionable fraud in Texas are (1) that a material representation was made; (2) that it was false; (3) that, when the speaker made it, he knew it was false or made recklessly without any knowledge of its truth and as a positive assertion; (4) that they made it with the intention that it should be acted upon by the party; (5) that the party acted in reliance upon it; and (6) that he thereby suffered injury. ***South Hampton Co. v. Stinnes Corp.***, 733 F.2d 1108 (5th Cir. 1984); ***Trenholm v. Ratcliff***, 646 S.W.2d 927 (Tex. 1983). As discussed above, Plaintiffs admitted in deposition that neither HPC nor O'Donnell made any representations to them and, consequently, any misrepresentations. McDonald dep. Vol. VI at 1062-66; Topalian dep. at 151; Garcia-Quiroga dep. at 159; Law dep. at 76; Burroughs dep. at 84-85; LaCelle dep. at 157-63, 168-69. Because Plaintiffs cannot establish this element necessary to establish common law fraud, HPC and O'Donnell are entitled to summary judgment.

IX. HPC AND O'DONNELL DID NOT VIOLATE THE RICO ACT

Plaintiffs assert RICO claims against HPC and O'Donnell based upon allegations of illegal kickbacks and inflated contractual drilling prices. 18 U.S.C. § 1961 *et seq.* (1982). RICO prohibits four forms of activity: (1) investment in an enterprise engaged in or affecting interstate or foreign commerce of income obtained through a pattern of racketeering or through collection of an unlawful debt; (2) acquisition of an interest in such an enterprise

through a pattern of racketeering or through collection of an unlawful debt; (3) conduct of the affairs of such an enterprise through a pattern of racketeering or through collection of an unlawful debt; and (4) conspiracy to violate any of these three provisions. Civil remedies are available for violations of Section 1962 to persons injured "by reason of" such RICO activities. Plaintiffs' claims must fail because they cannot establish any of the essential elements of RICO and Plaintiffs have no standing to assert RICO against HPC and O'Donnell.

A. Plaintiffs Cannot Establish the Activities Prohibited Under RICO

To establish a violation of § 1962(a), the Plaintiffs must establish that HPC or O'Donnell "derived income" from a "pattern" of "racketeering activity" in which they participated as principals; and that they used or invested that income to acquire an interest in, establish or operate the enterprise. ***H.J., Inc. v. Northwestern Bell Telephone Company***, 648 F. Supp. 419, 428 n.7 (D. Minn. 1986). After extensive discovery, Plaintiffs cannot provide any evidence that either HPC or O'Donnell used or invested income derived from any pattern of racketeering activity in Onshore for any purpose. In fact, HPC and O'Donnell had no financial interest in Onshore. *See* O'Donnell Affidavit.

Under 1962(b), the Plaintiffs must establish that HPC and O'Donnell "acquired or maintained" an interest or "control" of the enterprise through a "pattern" of "racketeering activity." The object of the activity must be to gain the interest or acquire control. Control is not limited by stock or capital ownership but may exist when the defendant has some meaningful ability to direct or influence the affairs or actions of the enterprise. *See, e.g.*, ***Sutliff, Inc. v. Donovan Cos.***, 727 F.2d 648, 653 (7th Cir. 1984). Again,

there is no evidence that either HPC or O'Donnell gained an interest or controlled the affairs or actions of Onshore. The only evidence is to the contrary. *See* O'Donnell Affidavit.

To establish a violation of § 1962(c), the Plaintiffs must establish that HPC and O'Donnell were "employed by or associated with" the enterprise and "conducted" or "participated" in the conduct of the affairs of the enterprise through a pattern of racketeering activity. ***Montesano v. Seafirst Commercial Corp.***, 818 F.2d 423, 424 (5th Cir. 1987). To satisfy the conduct element, this Court has held that the person must be able to commit the predicate offenses solely by virtue of his position in the enterprise, or the predicate offenses must be related to the activities of that enterprise. ***United States v. Cauble***, 706 F.2d 1322, 1341 (5th Cir. 1983), *cert. denied*, 465 U.S. 1005 (1984). The ***Cauble*** court, adopted the following test:

> A defendant does not "conduct" or "participate in the conduct" of a lawful enterprise's affairs, unless (1) the defendant has in fact committed the racketeering acts as alleged; (2) the defendant's position in the enterprise facilitated his commission of the racketeering acts, and (3) the predicate acts had some effect on the lawful enterprise.

Id. at 1332-33. Plaintiffs have been unable to provide any evidence that HPC or O'Donnell had any position with Onshore that facilitated the commission of any alleged predicate acts. The only evidence is to the contrary. *See* O'Donnell Affidavit.

Section 1962(d) makes it unlawful to conspire to violate § 1962(a), (b), or (c). To establish a violation of § 1962(d), Plaintiffs must establish that: (1) two or more

persons entered into an unlawful agreement to violate § 1962(a), (b), or (c), as those offenses have previously been defined; (2) HPC and O'Donnell knowingly and willfully became members of the conspiracy; (3) HPC and O'Donnell agreed to commit at least two of the acts of racketeering activity alleged by Plaintiffs to create a pattern; and (4) one of the members of the conspiracy knowingly committed at least one overt act in furtherance of the conspiracy alleged. ***United States v. Cauble***, 706 F.2d at 1341; ***United States v. Phillips***, 664 F.2d 971, 1012 (5th Cir. 1981), *cert. denied*, 459 U.S. 906 (1982); ***United States v. Elliott***, 571 F.2d 880, 902-03 (5th Cir.), *cert. denied*, 439 U.S. 953 (1978). Plaintiffs must establish that HPC and O'Donnell objectively manifested intent to participate in the affairs of the enterprise. ***Cauble***, 706 F.2d at 1341. Plaintiffs have been unable to provide any evidence nor is there any evidence that either HPC or O'Donnell knowingly and willfully became a member of any alleged conspiracy. The only evidence is to the contrary. *See* O'Donnell Affidavit.

B. Plaintiffs Cannot Establish the Existence of a RICO Enterprise

Plaintiffs' claims must be dismissed because there is no proof to support their allegations that Onshore is the RICO enterprise. The existence of an "enterprise" is a crucial element of Plaintiffs' RICO claim. *See* ***Sedima S.P.R.L v. Imrex Co., Inc.***, 473 U.S. 479, 496-97 (1985); ***United States v. Turkette***, 452 U.S. 576, 583 (1981). An "enterprise" includes any "individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity." 18 U.S.C. § 1961(4). The Supreme Court defined an "enterprise" in the context of § 1962:

> The enterprise is an entity, for present purposes a group of persons associated together for a common purpose of engaging in a course of conduct[,] . . . proved by evidence of an ongoing organization, formal or informal, and by evidence that the various associates function as a continuing unit. . . . The "enterprise" is not the "pattern of racketeering activity"; it is an entity separate and apart from the pattern of activity in which it engages.

452 U.S. at 583. This Court defined "enterprise" as requiring, in addition:

> the existence of a decision making structure, whether hierarchial or consensual. The RICO enterprise must have a common or shared purpose and continuity of structure and personnel.

Shaffer v. Williams, 794 F.2d 1030, 1032 (5th Cir. 1986) (citations omitted). To establish an "association in fact" enterprise, a plaintiff must show (1) an ongoing organization, formal or informal, (2) the association had a common purpose of engaging in a course of conduct, and (3) its various members functioned as a continuing unit. ***Turkette***, 452 U.S. at 583; ***Montesano v. Seafirst Commercial Corp.***, 818 F.2d 423, 427 (5th Cir. 1987); ***Shaffer***, 794 F.2d at 1032.

This Court also recently elaborated on the distinction between the pattern and the enterprise:

> When the alleged section 1962(c) violator is a legal entity, such as a corporation, this required separation is not

> established merely by showing that the corporation, through its employees, officers, and/or directors, committed a pattern of predicate acts in the conduct of its own business. [citation omitted] Nor does the fact that individual officers and employees of a corporation, in the course of their employment associate together and commit in the conduct of the corporation's business a pattern of predicate acts in its name and on its behalf, suffice to constitute such officers and employees (alone or together with the corporation itself) an association in fact enterprise distinct from the corporation. And, in ***Montesano*** we also explained that a RICO plaintiff must plead specific facts that establish an association that exists other than merely to commit the predicate acts that show pattern.

Old Time Enters., Inc. v. International Coffee Corp., 862 F.2d 1213, 1217-18 (5th Cir. 1989). The Plaintiffs' allegations in their response to the District Court's RICO Standing Order identifies the enterprise as Onshore. *See* **Plaintiffs' Response to RICO Standing Order** at 31 ¶ 6(a). There is no evidence to support the contention that Onshore functioned for the common purpose other than conduct of its own business. Neither is there any proof of any association-in-fact among the various Defendants that includes HPC or O'Donnell. *See* O'Donnell Affidavit. Thus, Plaintiffs have brought forth no evidence establishing the existence of a RICO enterprise.

C. Plaintiffs Cannot Establish a Pattern of Racketeering Activity

Plaintiffs' RICO claims should be denied because they have not established that Defendants committed a pattern of racketeering activity. A "pattern" of racketeering activity "requires at least two acts of racketeering activity." 18 U.S.C. § 1961(5) (1982). The Supreme Court in ***Sedima*** gave some insight to the "pattern" requirement:

> [A] pattern "requires at least two acts of racketeering activity," § 1961(5) (emphasis added), not that it "means" two such acts. The implication is that while two acts are necessary, they may not be sufficient. Indeed, in common parlance two of anything do not generally form a "pattern." The legislative history supports the view that two isolated acts of racketeering activity do not constitute a pattern. As the Senate Report explained: "The target of [RICO] is thus not sporadic activity. The infiltration of legitimate business normally requires more than one 'racketeering activity' and the threat of continuing activity to be effective. It is this factor of continuity plus relationship which combines to produce a pattern." . . . Significantly, in defining "pattern" in a later provision of the same bill, Congress was more enlightening: "criminal conduct forms a pattern if it embraces criminal acts that have the same or similar purposes, results, participants, victims, or methods of commission, or otherwise are interrelated by distinguishing characteristics and are not isolated events."

473 U.S. at 496 n.14 (citations omitted).

Since ***Sedima***, the great weight of authority has required a rigorous showing on this element. *See* ***Smith v. Ayres***, 845 F.2d 1360, 1365-66 n.18 (5th Cir. 1988); ***Crocker v. FDIC***, 826 F.2d 347, 348 n.2 (5th Cir. 1987), *cert. denied*, 108 S. Ct. 1075 (1988); ***Montesano v. Seafirst Commercial Corp.***, 818 F.2d 423, 426 (5th Cir. 1987); ***Smoky Greenhaw Cotton Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.***, 785 F.2d 1274, 1280-81 n.7 (5th Cir. 1986), *cert. denied*, 482 U.S. 928 (1987). Thus, Plaintiffs must establish at least two predicate acts of racketeering activity, which are indictable as defined in the 18 U.S.C. § 1961(1)(A), that show "continuity plus relationship" with the legitimate business. ***Old Time Enters., Inc.***, 862 F.2d at 1217. Plaintiffs' allegations fail to meet this "continuity plus relationship" test. Plaintiffs allege that HPC paid kickbacks to Johnson and overcharged Onshore. There is no proof that these alleged acts were anything other than isolated instances.

Moreover, Plaintiffs have no evidence that the alleged "predicate acts" constitute kickbacks or that HPC overcharged Onshore. RICO's definition of racketeering activity contains a laundry list of offenses which constitute the predicate acts necessary to establish a violation. 18 U.S.C. § 1961(1). Such acts must be acts "indictable" or "punishable" under one of several listed federal criminal laws or "chargeable" under a listed state law. ***Id.*** § 1961(1)(A). The alleged kickbacks were payments from HPC to Johnson arising from transactions wholly unrelated to Onshore. *See* O'Donnell Affidavit. As Johnson testified, the transactions transpired prior to his affiliation with Onshore. Johnson dep. at 32, 35-36, 24. Johnson confirms that such payments were not kickbacks. Johnson dep. at 77. Likewise, the auditor hired to review HPC's books and records testified that he found no evidence that the payments were kickbacks. Leggio dep. at 242-44. Furthermore, the alleged overcharges are

consistent with market prices and the contractual agreement in existence between Onshore and HPC. *See* O'Donnell Affidavit. Thus, because Plaintiffs cannot establish that HPC committed "predicate acts" that constitute a "pattern" of racketeering activity, HPC and O'Donnell are entitled to summary judgment.

CONCLUSION

For the foregoing reasons, Defendants HPC and O'Donnell, respectfully pray that the Final Judgment of the District Court, granting their motion for summary judgment be upheld and that this Court deny Plaintiffs' request for partial summary judgment.

Respectfully submitted,

VINSON & ELKINS

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CERTIFICATE OF SERVICE

I hereby certify that on the 21st day of November, 1990, a true and correct copy of the foregoing Brief of Houston Petroleum Company and Richard O'Donnell as Appellees has been forwarded to counsel of record for Appellant, by certified mail, return receipt requested.

_____

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